

Economic Update, March 3, 2017  
Submitted by Reuben Kyle

Summary: It was a busy week for economic news and most of it was good. Some reports indicated a slight backdown from earlier peaks, but housing, motor vehicle sales, and manufacturing and service sector activity remain at high levels. A number of measures of the manufacturing sector point to expansion after a period of doldrums at the end of 2016. Labor market indicators—unemployment rates, job creation trends, and initial claims—remain strong although the reports of labor shortages in skilled crafts continue. The only real negative report was the 4<sup>th</sup> quarter GDP growth rate, and the early indicators for Q1 2017 look strong.

Census Bureau

Monday, [Advance Report on Manufacturers' Shipments, Inventories, and Orders](#): In January 2017, new orders for manufactured durable goods increased by 1.8% from December, led by a 6.0% increase in new orders for transportation equipment. Shipments for manufactured durables fell by 0.1%, prompted by a 1.6% decrease in shipments of machinery. Unfilled orders also declined by 0.4%. Inventories were unchanged. In the case of capital goods, new orders for nondefense goods increased while shipments, unfilled orders, and inventories declined. Defense capital goods saw increased new orders, shipments, and inventories but decreased unfilled orders.

Tuesday, [Advance Economic Indicator Report \(International Trade, Retail, and Wholesale\)](#): The following are the advance January 2017 reports for the three areas. The deficit in international trade in goods rose by \$4.9 billion as exports fell by \$0.4 billion and imports increased by \$4.4 billion. Wholesale inventories declined by 0.3% for the month but were 2.2% higher than in January 2016. Retail inventories increased by 0.8% from December and by 4.0% from a year earlier.

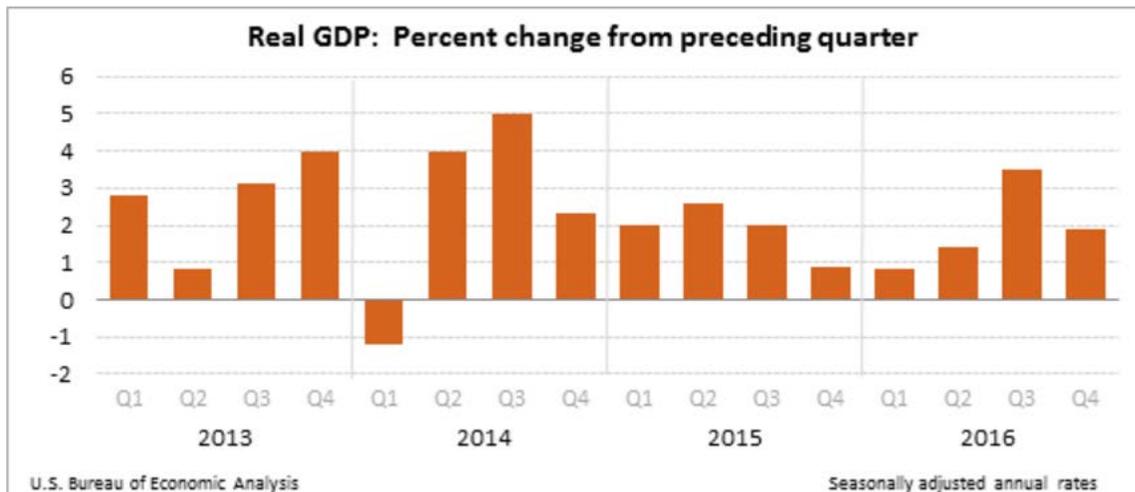
Wednesday, [Construction Spending](#): In January 2017, construction spending was down by 1.0% from December but was 3.1% higher than in January 2016. Residential spending was 0.5% above the prior month. In the public sector, education construction spending was 5.0% lower than in December, and highway construction was 3.3% lower.

Bureau of Labor Statistics

Tuesday, [Regional and State Unemployment \(Annual\)](#): In 2016, the annual average unemployment rate fell in 38 states and the District of Columbia, the rate increased in nine states, and it was unchanged in three. The lowest rate was 2.8% in both New Hampshire and South Dakota while the highest rate, 6.7%, was in New Mexico. Tennessee's average unemployment rate fell from 5.6% in 2015 to 4.8% in 2016 and that latter figure was below the national average of 4.9%. The employment-population ratio increased in 36 states and the District of Columbia, declined in 12 states, and was unchanged in two states. In Tennessee, the employment-population ratio rose from 56.2% in 2015 to 57.2% in 2016, and that latter figure was below the national average of 59.7%.

Bureau of Economic Analysis

Tuesday, [Gross Domestic Product, 4<sup>th</sup> Quarter 2016 and Annual \(2<sup>nd</sup> Estimate\)](#): Fourth quarter GDP grew at a rate of 1.9%, a rate unchanged from the advance estimate. "The increase in real GDP in the fourth quarter reflected positive contributions from personal consumption expenditures (PCE), private inventory investment, residential fixed investment, nonresidential fixed investment, and state and local government spending. These increases were partly offset by negative contributions from exports and federal government spending. Imports, which are a subtraction in the calculation of GDP, increased." The chart below shows the quarterly growth rates since 2013.



Wednesday, [Real Income and Outlays, January 2017](#): In current dollars Personal Income increased by 4.0% from December to January but inflation-adjusted Disposable Personal Income (DPI) fell by 0.2%. Real Personal Consumption Expenditures (PCE) was down by 0.3%. The PCE Price Index was 1.9% higher than in January 2016.

U.S. Department of Labor

Thursday, [Initial Claims](#): New Claims for unemployment insurance in the week ending February 25, 2017, fell by 19,000 to 233,000, and the four-week moving average dropped 6,250 to 234,250, which was the lowest level since April 14, 1973. The previous week, ending February 18, two states reported increases of 1,000 or more initial claims, and one state reported a decrease of 1,000 or more. Tennessee reported a decline of 436 new claims.

Board of Governors of the Federal Reserve

Wednesday, [Beige Book](#): The summary of the reports of the 12 Federal Reserve Districts stated the economic activity across the country continues to expand at a “modest to moderate pace” over the period from mid-January to mid-February. “A number of Districts noted that shortages of skilled workers—particularly engineers and IT workers—were driving up their wages, and there were also some reports of labor shortages in the leisure and hospitality, construction and manufacturing industries.” The Atlanta Federal Reserve Bank reporting on the 6<sup>th</sup> District found tightening labor markets with firms having difficulty finding workers in “various fields and skill levels.” Survey respondents expect unit costs to rise by 2% in the coming year. Online retail sales are growing while brick-and-mortar stores’ sales are “sluggish.” Across the District, hospitality providers reported growth compared with the last survey but there was no mention of Tennessee providers. Builders indicated that construction activity was higher than last year but that home sales were relatively flat. “Looking forward, the majority of District commercial real estate contacts expect the pace of nonresidential and multifamily construction activity to increase slightly over the next quarter.” Manufacturing activity has expanded since the last report with expectations of higher production levels over the next six months. In the Eighth District, or St. Louis Federal Reserve Bank, economic activity is reported as expanding at a modest pace. Employment has increased to the point that contacts in Memphis “reported an inability to fill key positions.” “Most general retailers reported a slight increase in year-over-year sales halfway through the first quarter. Similarly, the majority of hospitality contacts in St. Louis, Memphis, and Little Rock indicated that sales during this period met expectations and that they anticipate sustained growth in the months to come.” Manufacturing activity expanded with improvements since the last survey. Both residential real estate and construction activity improved “slightly” since the last report.

National Association of Realtors

Monday, [Pending Home Sales](#): In January 2017, the Pending Home Sales Index fell from 109.5 to 106.4, or 2.8%, and by 0.4% from January 2016. "Lawrence Yun, NAR chief economist, says home shoppers in January faced numerous obstacles in their quest to buy a home. 'The significant shortage of listings last month along with deteriorating affordability as the result of higher home prices and mortgage rates kept many would-be buyers at bay,...Buyer traffic is easily outpacing seller traffic in several metro areas and is why homes are selling at a much faster rate than a year ago. Most notably in the West, it's not uncommon to see a home come off the market within a month."

Standard & Poor's

Tuesday, [Corelogic Case-Shiller House Price Index](#): In December 2016, the annual rate of increase in the National Home Price Index was 5.8%, a 30-month high. "'Home prices continue to advance, with the national average rising faster than at any time in the last two-and-a-half years,'" says David M. Blitzer, Managing Director and Chairman of the Index Committee at S&P Dow Jones Indices. "With all 20 cities seeing prices rise over the last year, questions about whether this is a normal housing market or if prices could be heading for a fall are natural. In comparing current home price movements to history, it is necessary to adjust for inflation. Consumer prices are higher today than 20 or 30 years ago, while the inflation rate is lower. Looking at real or inflation adjusted home prices based on the S&P CoreLogic Case-Shiller National Index and the Consumer Price Index, the annual increase in home prices is currently 3.8%. Since 1975, the average pace is 1.3%; about two-thirds of the time, the rate is between -4% and +7%. Home prices are rising, but the speed is not alarming."

Autodata.com

Wednesday, [Motor Vehicle Sales](#): In February 2017, the seasonally-adjusted, annual sales rate of light motor vehicles was 17.58 million units compared to 17.61 million in January. The sales of Tennessee assemblers were mixed. General Motors reported a 22.7% decline in car sales compared to February 2016. Nissan reported a 12.0% drop in car sales year-over-year. Volkswagen reported a 12.7% increase in sales compared with 2016 and a 14.8% in year-to-date sales compared with the previous year.

The Conference Board

Tuesday, [Consumer Confidence Index](#): In February 2017, the index increased from 111.6 to 114.8. Lynn Franco, Director of Economic Indicators at The Conference Board is quoted: "Consumer confidence increased in February and remains at a 15-year high (July 2001, 116.3),... Consumers rated current business and labor market conditions more favorably this month than in January."

Bloomberg.com

Thursday, [Consumer Comfort Index](#): The latest index was 49.8 up from 48.0 the previous week. "Tuesday's consumer confidence index showed enormous strength as does today's consumer comfort index which jumped nearly 2 points in the February 26 week to 49.8 and a new high for the economic cycle. Record gains in confidence, however, have to result in significant gains for consumer spending."

Institute for Supply Management

Wednesday, [February 2017 Manufacturing ISM Report on Business](#): The index was 57.7% up 1.7 percentage points from 56.0% in January. The survey covers 18 manufacturing industry sectors of which 17 reported expanding and one reported contracting in February. The overall economy expanded for the 91st consecutive month. A few of respondents' comments were included:

- "Business [is] improving and lead times are extending by two or more weeks." (Chemical Products)

- “Very positive outlook for this quarter. Production goals have been adjusted multiple times and increased each time due to demand.” (Computer & Electronic Products)
- “Product demand continues to be solid.” (Plastics & Rubber Products)
- “Bookings are heavy early in the season. Expect robust first half of the year.” (Primary Metals)

Friday, [February 2017 Non-Manufacturing ISM Report on Business](#): The Non-manufacturing index (NMI) is 57.6% up by 1.1 percentage points from the January reading of 56.5% and marking the 86<sup>th</sup> consecutive month of expansion. Sixteen of the 18 industry sectors surveyed reported expanding, and two reported contracting. The table below gives details for both the manufacturing and non-manufacturing surveys.

ISM® NON-MANUFACTURING SURVEY RESULTS AT A GLANCE COMPARISON OF ISM® NON-MANUFACTURING AND ISM® MANUFACTURING SURVEYS* FEBRUARY 2017									
	Non-Manufacturing						Manufacturing		
Index	Series Index Feb	Series Index Jan	Percent Point Change	Direction	Rate of Change	Trend** (Months)	Series Index Feb	Series Index Jan	Percent Point Change
NMI®/PMI®	57.6	56.5	+1.1	Growing	Faster	86	57.7	56.0	+1.7
Business Activity/Production	63.6	60.3	+3.3	Growing	Faster	91	62.9	61.4	+1.5
New Orders	61.2	58.6	+2.6	Growing	Faster	91	65.1	60.4	+4.7
Employment	55.2	54.7	+0.5	Growing	Faster	36	54.2	56.1	-1.9
Supplier Deliveries	50.5	52.5	-2.0	Slowing	Slower	14	54.8	53.6	+1.2
Inventories	52.0	48.0	+4.0	Growing	From Contracting	1	51.5	48.5	+3.0
Prices	57.7	59.0	-1.3	Increasing	Slower	11	68.0	69.0	-1.0
Backlog of Orders	54.0	50.0	+4.0	Growing	From Unchanged	1	57.0	49.5	+7.5
New Export Orders	57.0	48.0	+9.0	Growing	From Contracting	1	55.0	54.5	+0.5
Imports	51.0	54.0	-3.0	Growing	Slower	2	54.0	50.0	+4.0
Inventory Sentiment	64.5	62.0	+2.5	Too High	Faster	237	N/A	N/A	N/A
Customers' Inventories	N/A	N/A	N/A	N/A	N/A	N/A	47.5	48.5	-1.0
<b>Overall Economy</b>				Growing	Faster	91			
<b>Non-Manufacturing Sector</b>				Growing	Faster	86			

\* **Non-Manufacturing ISM® Report On Business®** data is seasonally adjusted for Business Activity, New Orders, Prices and Employment Indexes. **Manufacturing ISM® Report On Business®** data is seasonally adjusted for New Orders, Production, Employment and Supplier Deliveries.

\*\* Number of months moving in current direction.

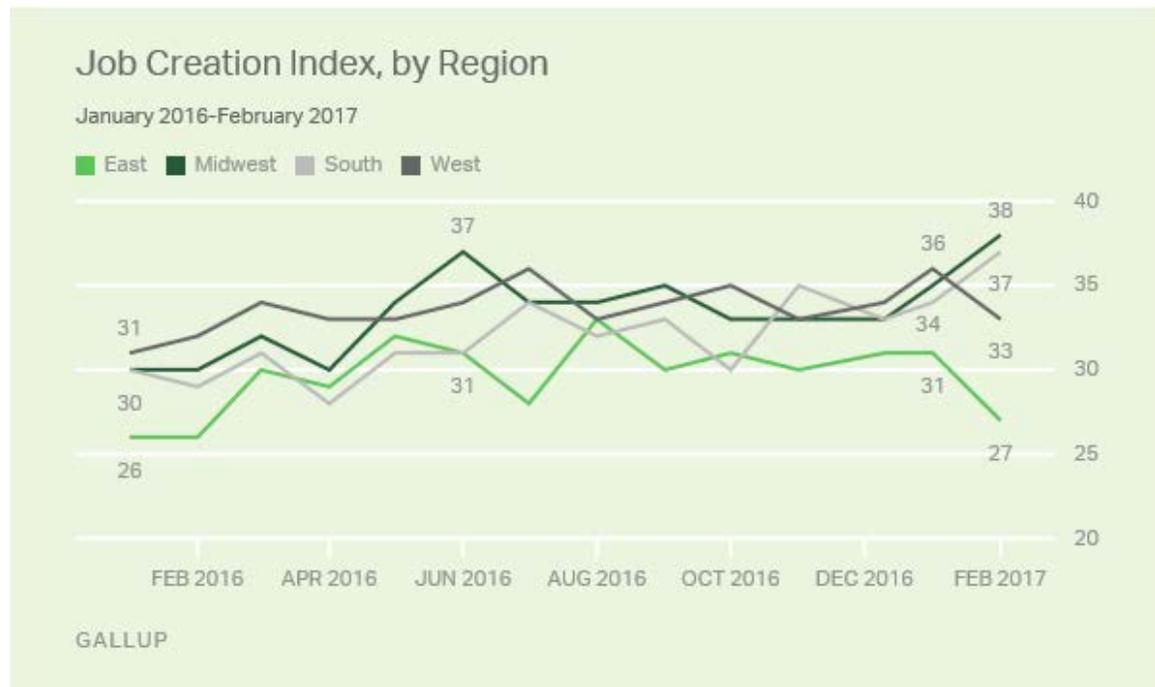
Markit Economics

Wednesday, [Purchasing Managers' Index \(PMI\) Manufacturing Index](#):. This index as 54.2 in February 2017, down from 55.0 in January. "As a result, the average reading for Q1 to date indicates that the manufacturing sector is on course to register its strongest quarterly improvement in business conditions for two years." Chris Williamson, Markit's Chief Economist, stated: "Growth is being driven by robust domestic demand, stemming in turn from buoyant consumers and increased investment spending by the energy sector in particular. Manufacturing is far from booming, however, as the strong dollar means near-stagnant exports continue to act as a drag on growth."

Friday, [PMI Services Index](#): In February 2017, this index fell from a 14-month high of 55.6 to 53.8. Economist Williamson wrote: "Taken together, the PMI survey readings for the first two months of the year suggest the economy is growing in the first quarter at a respectable annualised rate approaching 2.5%....The February survey is broadly consistent with 175,000 payroll jobs being added, which represents a pace of hiring that will do little to deter the Fed from delaying its next rate hike."

Gallup.com

Wednesday, [Job Creation Index](#): The February 2017 job creation index was +35 compared with +34 in January. "U.S. workers' perceptions of hiring activity reached a nine-year high in February, with many more employees saying their workplace is hiring people rather than letting workers go." However, the index varies across regions of the country. The graphic below shows that in the East the index is +27 compared with +38 in the West.



The Wall Street Journal

Monday, [Economic Forecasting Survey](#): The February 2017 survey of 76 economic forecasting individuals and organizations received 62 responses. The average projection of 4<sup>th</sup> quarter GDP growth is 2.0% and for the 1<sup>st</sup> quarter of 2017 it is 2.2%. (See above for the BEA's estimate of Q4 2016 growth.) The forecast Consumer Price Index for June 2017 is 2.4% and 2.3% for December of this year. For June 2017, the average forecast price of oil is \$54.29 while the current price, as this is written, is \$54.14. And oil prices are forecast to rise slowly to \$55.79 by the end of the year. The unemployment rate is forecast

to be 4.6% by June of this year and 4.5% by December 2017. Nonfarm payrolls are expected to add 175,000 jobs per month this year. Housing starts are forecast at 1.26 million for the year as in the beginning of 2017 and rising to 1.35 million in 2018. The increase in house prices is forecast to drop from 5.6% to 4.6% in 2017 and to 3.8% by year's end. The yield on 10-year Treasury notes is forecast to rise slightly to 2.62% by June 2017 and to 2.86% by December 2017. One-quarter of the respondents expect a further rise in the federal funds rate in March and 96.8% expect one by June of 2017. So, the fed funds rate is forecast to be 1.31% by December 2017 and 1.71% by June 2018. Respondents assess the probability of a recession in the next 12 months at 15%, with roughly half of them seeing an upside risk for their GDP growth forecasts.

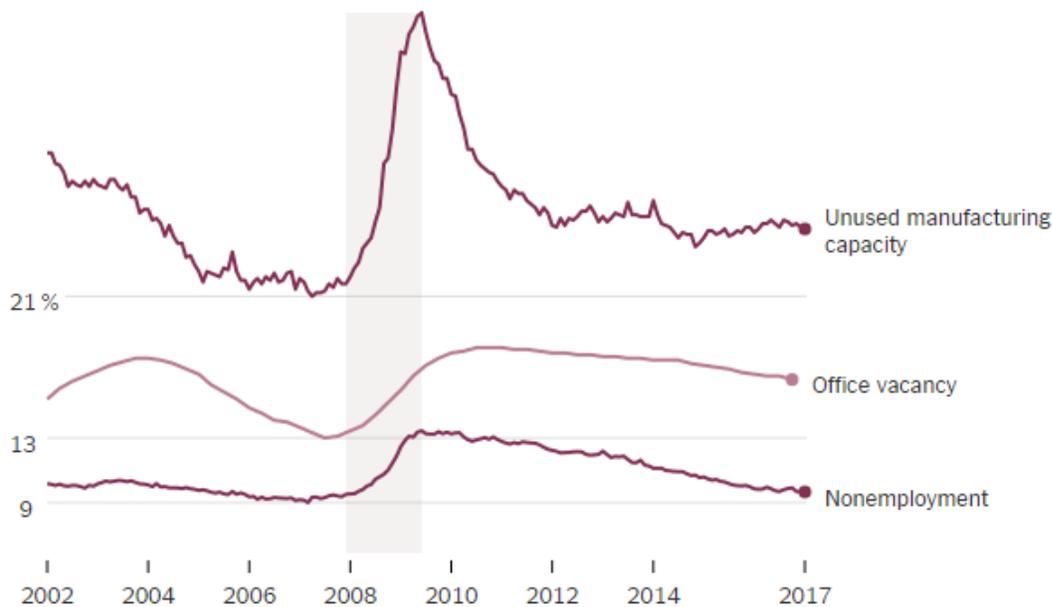
The New York Times

Monday, [The Big Question for the U.S. Economy: How Much Room Is There to Grow?](#): This article attempts to assess just how much slack there is in the economy. The conclusion is that there is some slack which could allow a faster rate of GDP growth without fostering inflation. The graphic below illustrates the point of the article.

## Empty Buildings, Idle Machines

Three measures that show slack in the United States economy isn't back to mid-2000s levels.

Percent unused capacity



Gray lines indicate low point of each series since 2002. Unused manufacturing capacity is the inverse of capacity utilization; nonemployment is Hornstein-Kudlyak-Lange Nonemployment index.

Source: Federal Reserve Board, Reis, Federal Reserve Bank of Richmond