U.S. Economy in a Snapshot
Research & Statistics Group
August 2015

The U.S. Economy in a Snapshot compiles observations of staff members of the Federal Reserve Bank of New York’s Research and Statistics Group. The views, model results, and analysis presented are solely those of the individual contributors and do not necessarily reflect the position of the Federal Reserve Bank of New York or the Federal Reserve System. The analysis presented herein is based on data released through August 14, 2015.
- Consumer spending rebounded from a weak first quarter, although the pattern of monthly growth remains choppy.
  - Real consumption expenditures were flat in June, but they grew at a healthy rate during the second quarter overall.

- Business equipment spending fell in the second quarter, the second decline in the last 3 quarters.
  - Business investment in structures also fell in the second quarter, but at a slower pace than in the first quarter.

- There are signs of further improvement in housing market conditions.

- July payroll growth was again solid, although there was no change in the unemployment rate, the labor force participation rate, and the employment-population ratio.
  - Wage growth remains subdued relative to pre-recession levels.

- Inflation remained well below the FOMC’s longer-term objective.

- Financial markets signaled greater concern about the global growth outlook, marked by a notable downturn in commodity prices. China’s recent devaluation of the yuan put further downward pressure on commodity prices.

### Output remains below its potential level

- GDP growth in this expansion has been subdued compared to previous expansions.
  - This trend continued in 2015Q2: real GDP increased 2.3% (annual rate) in the quarter, a moderate rebound from the weak growth (0.6%) in 2015Q1.

- The gap between real GDP and the Congressional Budget Office’s measure of real potential GDP was almost 3% in 2015Q2.
  - Resource slack by this measure continues to appear larger than that implied by most estimates of the unemployment gap.

- Continued low inflation appears consistent with the economy operating below potential.
**Labor Market Indicators**

- **Further improvement in the labor market**
  - The July labor market report indicated ongoing improvement in labor market conditions, with nonfarm payroll employment increasing by 215,000.
  - Despite the continued solid payroll gains, the major household survey indicators were unchanged in July.
    - The unemployment rate held steady at 5.3%. The labor force participation rate remained at 62.6% and the employment-population ratio was unchanged at 59.3%.

---

**PCE Deflator**

- **Inflation remains low**
  - For the three months through June, the total PCE deflator increased at a 2.4% annual rate, while the core PCE deflator (which excludes food and energy prices) rose at a 1.7% rate.
  - On a 12 month change basis, both measures have been fairly stable since the beginning of the year at levels significantly below the FOMC's longer-run objective of 2%.
  - A slowing of health services inflation and declining durable goods prices have been factors restraining core inflation in recent years, but these effects dissipated during the second quarter.
Output growth strengthens in Q2

- According to the advance release, GDP grew at a 2.3% annual rate in Q2.
  - The pace of output growth in Q2 improved from 0.6% in Q1, with first quarter growth being revised up from a previously reported decline of 0.2%.
  - The pickup in growth supports the view that temporary factors were responsible for some of the weakness during the first quarter.

- The acceleration in real GDP growth reflects stronger growth in consumer spending and a narrower trade deficit, partially offset by a decline in business fixed investment and a modest slowing in inventory investment.

Real growth of recent years revised downward

- The latest GDP release included the annual revisions: real GDP in recent years was revised downward.
  - Real GDP growth between 2011Q4 and 2015Q1 was revised down from 2.2% (annual rate) to 2.0%.

- A lowering of consumption expenditures was the primary factor in the downward GDP revision.
  - State and local government expenditures were also revised down.

- Real gross domestic income (GDI) was revised downward: its growth over 2011Q4 – 2015Q2 is now estimated to be 2.3%, down from 2.7% previously.
  - The statistical discrepancy narrowed, but is still wide relative to historical norms, with GDI larger than GDP.
**Households**

**Disposable Income, Consumption, and Wealth**

- Real consumption expenditures grew a healthy 2.9% in the second quarter.
  - While consumption spending was flat in June, it was more than offset by strength in the previous two months.

- Household fundamentals remained strong.
  - Real disposable income grew 0.2% in June, similar to the pace in the previous two months.
  - Household net worth is approaching its pre-recession peak.

- The personal saving rate ticked up from 4.6% in May to 4.8% in June.
  - The saving rate was 4.8% in Q2, down from 5.2% in Q1.

**Monthly goods spending remains uneven**

- Looking behind the solid growth in Q2, monthly consumer spending on goods continues to display a choppy pattern.
  - Overall goods consumption declined 0.4% in June, after increasing 1.0% in May.
  - Durable consumption declined 1.1% in June, after increasing 1.3% in May.
  - Nondurables spending was flat in June, after increasing 0.9% in May.

- Service consumption continued to grow at a steady, but moderate, pace.
**Business Sector**

**Equipment Investment and Capacity Utilization**

- Real business investment in new equipment declined at a 4.1% annual rate in 2015Q2, after rising 2.3% in Q1.
  - Business equipment spending has declined twice during the past three quarters. Over the past four quarters, business equipment spending has only grown 2.1%.
  - Historically, the rate of growth of business spending on new equipment has been positively correlated with the manufacturing capacity utilization rate.
  - The manufacturing capacity utilization rate remained unchanged at 75.9% in 2015Q2, after declining in the first quarter. It remains below the levels that prevailed prior to the recession.

**Investment in Nonresidential Structures**

- Real business investment in new structures has been declining since the beginning of the year. Growth in real business investment in new structures over 2014Q2 – 2015Q2 is now estimated to be -1.7%.
  - Investment in petroleum and natural gas drilling rigs is an important component of overall business investment in nonresidential structures.
  - Spending on new structures in the petroleum and natural gas sector has collapsed since the beginning of the year. Over the first half of 2015, real investment in oil and gas structures is down at nearly a 60% annual rate.
**Total housing starts at highest level since 2007Q4**

- Total housing starts reached 1.144 million units (annual rate) in 2015Q2, the highest level since 2007Q4.
- The multifamily sector continued to lead the way. Multifamily starts averaged 441,000 (annual rate) in 2015Q2, the highest since the first quarter of 1989.
- In contrast, single family starts averaged just 700,000 (annual rate) in 2015Q2, about the same as in 2014Q4, despite low mortgage interest rates.

**Home price increases show recent pickup**

- The CoreLogic single family national home price index rose 6.5% in June from the previous year, the highest increase since June 2014.
- After falling sharply from April 2006 through February 2012, this national home price index is now only 11% below its peak value.
- One factor influencing home prices is the inventory of homes for sale (expressed as the number of months supply at the current sales pace).
  - The current measure is relatively low, creating an environment of price appreciation given the current configuration of low mortgage interest rates and an improving labor market.
**GOVERNMENT SECTOR**

**Real Government Consumption and Gross Investment**

- Total real government consumption and gross investment is now growing modestly on a four quarter change basis after a 3½ year period during which it was contracting.
  - Over the past four quarters, total government contribution to growth of real GDP has been a modest 0.1 percentage point.

- Real consumption and gross investment at the federal level fell at a 0.6% rate over the four quarters ending in 2015Q2, the smallest decline since 2011Q1.

- Real consumption and gross investment at the state and local level grew 0.8% over the four quarters ending in 2015Q2, continuing the modest expansion since early 2014.
  - The state and local sector represents over 60% of total government consumption and gross investment.

**State and local investment begins to gain footing**

- State and local government gross investment had a relatively strong second quarter, and is now only 17% below its 2008 peak.

- Compared to consumption, investment declined more steeply in the recession and is taking longer to recover.
  - Larger spending items including education, transportation, and highway construction showed marked growth in Q2.

- Consumption expenditures continue to grow at a steady, albeit modest, pace.
  - Consumption expenditures, comprised largely of employee compensation, account for about 80% of state and local spending and has grown steadily but modestly in 2015.
INTERNATIONAL DEVELOPMENTS

Net Exports: Contribution to GDP Growth

Positive net exports growth contribution in Q2

- Net exports added 0.1 percentage point to GDP growth in 2015Q2, following a 1.9 percentage point drag in Q1.

- Real export growth has remained weak during 2015, as growth in Q2 did not fully offset the sharp decline in Q1.
  - Over the year, real exports were up only 1.5%.
  - Overall weakness in exports is mainly attributed to the strong US dollar.

- Growth in real nonoil imports was moderate in Q2 following strong growth during the previous two quarters.
  - Real nonoil goods imports have experienced positive growth for 10 consecutive quarters.

Commodity prices are falling

- Slower growth in China and lower oil prices are putting downward pressure on commodity prices.
  - The drop is most pronounced for metals, with a more modest downward trend for industrial supplies.

- The CRB metal index is down 25% over the year, with copper, steel, tin, and zinc all down by 20% to 25%.
  - Iron ore is down 40%.

- The CRB raw industrial index is down 15% over the year.
  - Index includes some metals.
  - Cotton is down 5%, while rubber is down 15%.
**Payroll Employment and Aggregate Hours**

![Graph showing payroll employment and aggregate hours from 2000 to 2014 with shaded areas indicating NBER recessions.]

**Employment gains and hours growth remain solid**

- Nonfarm payroll employment increased by 215,000 in July.
  - Payroll employment increased on average by 235,000 in the last three months.
  - The pace of employment gains was very similar to the improvement in the 12 months prior to July, with employment gains averaging 246,000 per month.

- With the solid rise in payroll employment and an increase in average weekly hours from 34.5 to 34.6 hours, aggregate hours worked increased by 0.5% in July.
  - The 12 month change in aggregate hours was 2.7%.

**Service-providing sector leads employment gains**

- Employment in goods-producing industries rose by 17,000 in July, while employment in private service-providing industries increased by 193,000.

- The one month diffusion index—reflecting the balance between industries increasing and decreasing employment—was 64.4 in July, near its average over the previous 12 months (63.6).
  - The diffusion index indicates that employment gains continued to be broad based across industries.
  - While the index has remained at fairly solid levels, it is still somewhat below the robust numbers seen last year.
Growth of Average Hourly Earnings: All Employees

Labor compensation growth remains subdued
- Average hourly earnings increased 0.2% July and increased 2.1% over the past 12 months.
  - The 12 month change is within the narrow range that has prevailed since the end of the recession.
- After increasing by 0.6% in 2015Q1, growth in the employment cost index (ECI) slowed to 0.2% in the second quarter.
  - The weaker growth in the ECI reflected payback from unusually strong wage and salary growth in Q1 for some high-paying industries and occupations, as well as a broad-based slowing in benefits growth.
  - The 12 month change was 2.0%.

Wage and Salary Compensation: Private Workers

Explaining recent volatility in the ECI
- The large swing in ECI growth in 2015 was unduly influenced by the incentive payments for highly compensated employees.
  - These payments were most noticeable in the professional and business services sector.
- After removing this sector’s contribution to overall ECI wage and salary growth, the 12 month growth in wage and salary compensation is more consistent with the gradual gains in the ECI seen over 2014.
INFLATION

Dollar Exchange Rate and Nonoil Import Prices

- Nonoil Import Prices (Right Axis)
- Dollar (Left Axis)

Source: Federal Reserve Board, Bureau of Labor Statistics, via Haver Analytics
Note: Dollar is Board's trade-weighted measure.

Import prices are falling

- The stronger dollar is putting downward pressure on nonoil import prices.
  - Foreign firms can cut prices on U.S. sales because their production costs in dollar terms are now lower.

- The dollar index is up 15% over the year and nonoil import prices are down 3%.
  - Import price indexes for autos, capital goods, and consumer goods are down 1%-2%.
  - The relatively small price declines imply foreign firms are experiencing much higher profit margins from their U.S. sales.

- Lower commodity prices have contributed to the 25% drop in the import price index for industrial supplies.

CPI Inflation: Core Goods and Core Services

- Core Services
- Core Goods

Source: Bureau of Labor Statistics, via Haver Analytics
Note: Shading shows NBER recessions.

Core services continue to anchor inflation

- Core CPI inflation rose 0.2% in June; its 12 month change increased to 1.8% from 1.7% in May.

- Core services inflation and core goods inflation continue to diverge by about 3 percentage points per year.
  - Core services prices are rising around 2.5% per year, while core good prices are declining by about 0.5%.
  - A gap of this magnitude between the two inflation series is not unusual.
FINANCIAL MARKETS

**European 10-Year Sovereign Yields**

- Yields on Greek government bonds declined sharply following a new agreement between Greece and its creditors in mid-July.
  - The yield on the 10-year bond declined from a previous high of 19.3% on July 8 to 11.9% on August 6.
- Italian government bond yields declined on positive news from Greece and strong bond auctions.
  - The 10-year yield declined from 2.3% on July 6 to 1.9% on August 6.
- As peripheral yields declined, German bond yields rose reversing flight to safety flows.

**International Equity Indices**

- U.S. stock markets increased modestly since the end of June and remain fairly close to record highs.
  - U.S. equity market volatility was subdued in July and remains at historically moderate-to-low levels.
- Chinese equity markets have rebounded, but remain volatile.
  - Starting from a low on July 8, the Hang Seng index gained 8.6% through July 21, but then gave up some gains and ended only 3.7% higher through August 6.
  - Volatility has remained high in the presence of policy announcements and mixed economic data.
**FINANCIAL MARKETS**

**10-Year Treasury and Term Premia**

- Against a backdrop of lower commodity prices and concerns about the global outlook, the 10-year Treasury zero coupon yield fell from 2.40% on July 6 to 2.29% on August 6.

- The recent decline in 10-year yields can be attributed to roughly equal declines in market-implied TIPS-based measures of long-term inflation expectations ("breakeven") and the inflation risk premium (as implied by the Adrian-Crump-Moench model).

**5-10 Year Forward Decomposition**

- Market-implied TIPS-based measures of long-term inflation expectations ("breakeven") have declined in recent weeks.
  - After reaching a recent high of 2.15% on July 7, the breakeven inflation rate declined to 1.93% on August 6.
  - The breakeven inflation rate remains at the low end of the range observed in recent years.

- Variation in the breakeven inflation rate appears largely driven by changes in the inflation risk premium, with implied expected inflation (as measured by the Adrian-Crump-Moench model) remaining fairly stable.
FINANCIAL MARKETS

Expected Fed Funds Rate

- The expected path for the Federal Funds rate implied by rates on overnight indexed swaps has flattened modestly since early July, moving the expected lift-off date somewhat forward.

- The market-implied path remains below the paths suggested by the median forecast in the FOMC's Summary of Economic Projections and the NY Fed Primary Dealer Survey.

Oil and Gold Prices

- Oil prices have continued to decline on concerns over global growth and persistent oversupply.
  - The price of the front month West Texas Intermediate crude futures declined 15% between July 6 and August 6.
  - Lower demand was associated with weak Chinese manufacturing data and lower growth expectations in other emerging markets.
  - Supply from OPEC continues to rise; U.S. producers are also sustaining higher than expected production amid cost cutting measures and efficiency gains.

- The price of gold dropped 6.7% from July 6 to August 6, continuing the trend of the last few months.
Mortgage Originations by Credit Score

- Mortgage originations are picking up
  - After a mini-refinancing boom in 2013, origination volume in 2014 dropped to a 14-year low.
  - Newly originated mortgages have now increased for four consecutive quarters.
  - The originations, however, are predominantly going to prime borrowers:
    - Of the newly originated mortgages in 2015Q2, half ($232 billion) were originated to borrowers with credit scores over 780.
    - By contrast, only 8%, or $38 billion, were originated to borrowers with credit scores below 660.

Credit Score at Origination: Mortgages

- Underwriting standards remain tight
  - Credit standards for mortgage lending tightened sharply between 2007 and mid-2009, and have loosened only slightly since 2012.
  - Between 1999 and 2007, 90 percent of borrowers who originated mortgages had credit scores above 590; between 2008 and 2015, 90 percent of borrowers had credit scores above 645.
  - As the distribution has shifted up, it has become more difficult for subprime borrowers to originate loans.
SPECIAL TOPIC - CONSUMER CREDIT PANEL

Percent of Loan Balance 90+ Days Delinquent

Delinquency rates continue to improve

- The delinquency rates for all products, excluding student loans, have improved considerably since the recession.

- With the decline in new subprime mortgage lending since 2009, the quality of outstanding mortgage debt has improved and has contributed to the improvement in mortgage delinquency rates.

New Foreclosures and Bankruptcies for Consumers

Foreclosures reach historical low

- About 95,000 consumers had a foreclosure notation added to their credit report in 2015Q2, the fewest in the 16-year history of the data.
  - Since reaching a peak of 566,000 in 2009Q2, foreclosure notations have shown a considerable and fairly steady decline.

- New bankruptcies have also slowed and returned to levels last seen during 2006.

Source: FRBNY Consumer Credit Panel/Equifax