Nationwide Economics

Weekly Economic Review & Outlook

October 25, 2021

More mixed housing data imply continued supply constraints

Last week's economic data continued to show supply-side problems, but equity markets seemed to brush it off. The S&P 500 index finished the week just below a record high (which it set the day before) after falling by roughly five percent over the prior month and a half. Moreover, longer-term interest rates continued their recent upward move, climbing to near the expansion highs set in March.

Existing home sales rose sharply

Existing home sales jumped by 7.0 percent for September to an annualized pace of 6.29 million units. This jump was accompanied by a decrease in the inventory-sales ratio and leaves the months' supply at just 2.4 versus a long-term average of 4.7. The median price of an existing home sold fell for the third straight month (mostly from a change in the mix of where homes were sold) but over the past year prices are up by an unsustainable 13.3 percent. Positive fundamentals (strong job growth, low mortgage rates, etc.) have kept demand strong despite lack of supply and the rise in Covid cases over the past couple of months.

The Delta variant didn't hold consumers back from showing interest in new homes, either, helping to raise homebuilder sentiment last month. The NAHB housing market index rose from 76 to 80 in September, suggesting a high level of homebuilder sentiment. While this is certainly positive, there are still constraints that are holding back new home sales. Builder commentary showed that labor shortages and supply constraints are expected to continue to pressure sales and keep prices rising in the near term. This can be seen in last week's housing starts and building permits data for September. While the overall level of starts edged lower, this was driven by the volatile multifamily sector. Single-family starts, which are mostly for owner-occupied units, were flat for the month despite solid home sales and high builder optimism. Given the supply-side difficulties that homebuilders face, it will be difficult for starts to move significantly higher in the near term even if demand increases. The small drop in single-family building permits (a near-term leading indicator for starts) illustrates this. With demand remaining strong and limited supply continuing, upward pressure on home prices is likely to persist.

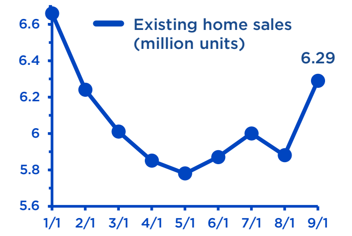
Equity markets remain resilient

The S&P 500 index rose by 1.6 percent last week and closed just below the all-time high it set on Thursday. This followed a drop of roughly five percent between September 2 and October 4. Corporate bond prices have also held up well despite being down on a year-to-date basis. The spread between investment grade corporate bonds and similar duration U.S. Treasury securities has been steady for a while. This spread is a measure of the market's expectation for corporate bond credit risk, and the fact that it hasn't widened despite growing concerns on inflation and slower third-quarter real GDP growth is a positive sign.

U.S. Treasury longer-term yields have been rising since early August, but especially since the mid-September FOMC meeting. This has occurred from a combination of higher inflation expectations, the Fed indicating a tapering of its QE purchases as soon as early November, and financial markets anticipating a sooner and more aggressive move in short-term rates by the Fed. The U.S. Treasury 10-year note yield rose by almost ten basis points last week to 1.66 percent. The futures market has priced in an expectation that the Fed will raise short term interest rates by a total of 50 basis points by the end of 2022.

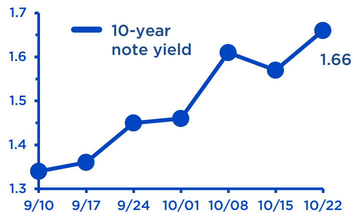
The rise in rates and the lack of a rise in investment grade corporate bond spreads suggest that financial markets brushed off weaker data from last week and instead concentrated on inflation and stronger economic data. While September industrial production fell by 1.3 percent mainly due to supply chain and weather impacts, the Conference Board's index of leading economic indicators rose by 0.2 percent for the month and by 9.3 percent over the past year, suggesting that there is little chance of a near-term economic downturn.

Existing home sales surprise to the upside



Existing home sales rose for September to an annualized pace of 6.29 million despite the Delta variant and limited supply.

U.S. Treasury 10-year note yield has been moving higher



Expectations for higher inflation as well as eventual monetary policy tightening by the Fed have combined to push 10-year Treasury yields to the highest levels since March.

Source: Haver Analytics

Contributors: Dan Hadden, Financial Markets Economist | Daniel Vielhaber, Economist

The Week Ahead

Here's what we are watching this week

New home sales
Oct 26

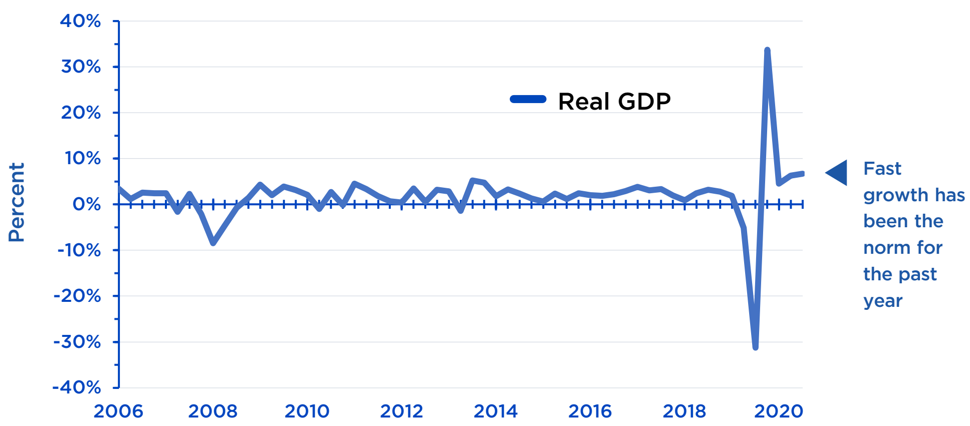
Small decline expected for new home sales

Although constrained by high input costs, labor shortages, supply chain problems, and lack of buildable lots, the pace of new home sales has remained solid although much lower than seen over the second half of last year and early this year. Low mortgage rates, strong job and wage growth, and an ongoing desire for "space" have supported housing demand, plus new homes likely continue to benefit from the extremely low number of existing homes for sale (which remained close to all-time lows in September). According to the MBA, mortgage applications for new homes fell in September, suggesting that reported new home sales should have declined, as well. We project a modest drop in the annualized pace of new home sales for September to 735,000 units.

Real GDP
Oct 28

Real GDP growth expected to slow sharply

While a few months ago consensus expectations for the annualized real GDP growth exceeded six percent, projections are now far lower. Supply chain disruptions have been more severe and longer lasting than anticipated, limiting production and inventories in many industries (e.g., automobiles). Furthermore, port bottlenecks have resulted in far weaker than expected exports. Additionally, persistently higher inflation accentuates that gap between real and nominal activity. Taken together, we project annualized third-quarter real GDP growth of 1.9 percent. While this is about the pace of trend growth pre-Covid, it is disappointingly slow with unemployment and capacity utilization still not at full employment levels.



Source: Bureau of Economic Analysis/Haver Analytics

Personal income and spending
Oct 29

Strong growth in personal income and consumer spending likely

Rising wages and a record-low layoff/discharge rate likely led to strong growth in personal income in September; we believe personal income grew by one percent, which would be the fastest growth not influenced by stimulus checks since December 2018. This plus another strong month for retail sales means probable strong growth in personal consumption expenditures (PCE) for the second straight month; we project PCE growth of 0.6 percent. Lastly, we project moderate growth of 0.2 percent in the core PCE price index, which would bring the 12-month trend rate up slightly to 3.7 percent.

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Weekly Market Snapshot

Provided by IMG Business and Product Development – Data Analytics Team

Equity	Last	Returns 1 Week	YTD*	1 Year*
S&P 500 (Large)	4,545	1.66%	22.39%	33.55%
S&P 400 (Mid)	2,797	1.78%	22.42%	41.42%
S&P 600 (Small)	1,381	1.27%	24.57%	50.51%
S&P 500 (High Quality)	52	2.56%	23.84%	32.63%
Russell 1000	4,912	1.69%	21.79%	34.31%
Russell 2000	5,694	1.14%	16.88%	41.95%
Dow Jones	35,677	1.12%	18.30%	28.21%
NASDAQ	15,090	1.30%	17.68%	32.04%
MSCI EAFE	2,339	0.63%	11.60%	28.20%
MSCI EM	1,293	0.75%	2.22%	16.48%

*represents total return

S&P Metrics	LTM P/E	NTM P/E	LTM EPS Growth	NTM EPS Growth
Current	23.29	20.96	33.73	15.39
Prior Month	23.34	20.56	27.97	18.44
Prior Year	24.24	21.64	-13.17	16.41

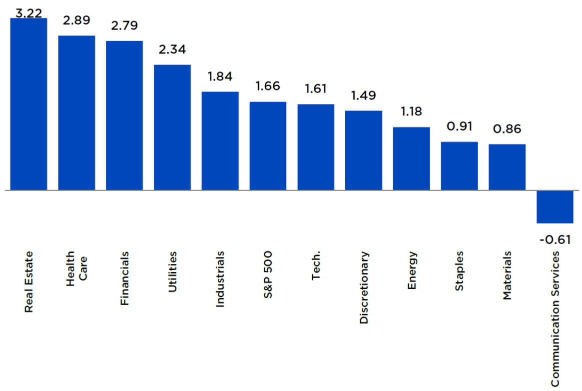
Fixed Income	Last	Returns 1 Week	YTD	1 Year
U.S. Aggregate	1.71%	-0.37%	-2.09%	-0.97%
U.S. Inv Grade	2.31%	-0.48%	-1.81%	1.20%
U.S. High Yield	4.79%	-0.08%	4.26%	9.31%
TIPS	1.37%	0.14%	4.67%	6.65%

Rates	Last	Change 1 Week	YTD	1 Year
6M T-Bill	0.07%	0.01	-0.02	-0.04
2 Yr Treasury	0.48%	0.07	0.35	0.32
5 Yr Treasury	1.22%	0.09	0.86	0.84
10 Yr Treasury	1.66%	0.07	0.73	0.79
30 Yr Treasury	2.08%	0.03	0.43	0.41

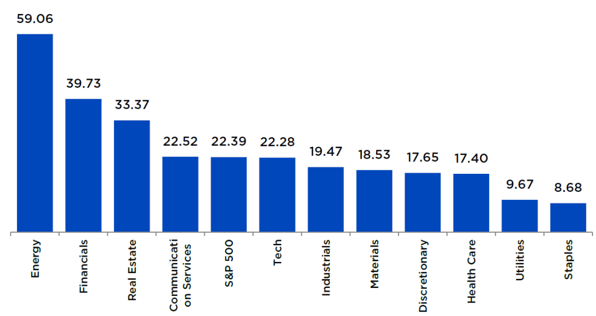
Spreads	Last	Change (Abs %) 1 Week	YTD	1 Year
AAA Rated	0.47	0.01	-0.08	-0.22
BBB Rated	1.13	0.00	-0.19	-0.55
High Yield	3.07	-0.05	-0.79	-1.81
10 to 2 yr Treasury	1.18	0.00	0.38	0.47

Commodities/FX	Last	Returns (Currencies in $ strength) 1 Week	YTD	1 Year
Gold	1795.50	1.60%	-5.16%	-5.55%
Bitcoin	60725.70	-1.19%	109.23%	368.20%
WTI Oil	83.76	1.66%	73.24%	107.02%
EUR/USD	1.16465	-0.35%	4.81%	1.53%
USD/JPY	113.59	-0.41%	10.02%	8.39%

S&P Sector Returns — Week (%)

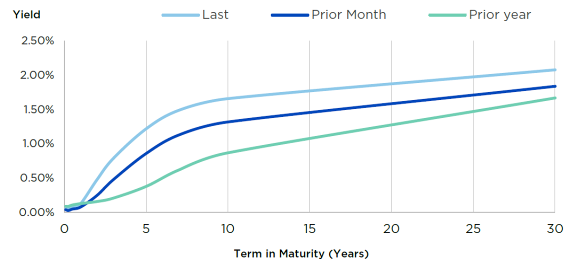


S&P Sector Returns — YTD (%)*



*represents total return

U.S. Yield Curve



Russell Style Returns — Week

	Value	Core	Growth
Large	1.6	1.7	1.8
Mid	1.8	2.0	2.4
Small	1.0	1.1	1.3

Russell Style Returns — YTD

	Value	Core	Growth
Large	22.6	21.8	21.1
Mid	25.7	22.5	16.7
Small	28.4	16.9	6.4

Source: FactSet

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Additional Economic Indicators

Previous Week's Indicators

	Period	Actual	Previous
Industrial production	Sept.	-1.3%	-0.1%
Capacity utilization	Sept.	75.2%	76.2%
NAHB housing market index	Oct.	80	76
Housing starts	Sept.	1.56 M	1.58 M
Building permits	Sept.	1.59 M	1.72 M
Initial jobless claims	Week ending Oct. 16	290,000	296,000
Philadelphia Fed manufacturing index	Oct.	23.8	30.7
Existing home sales	Sept.	6.29 M	5.88 M
Index of leading economic indicators	Sept.	0.2%	0.8%
Markit flash manufacturing index	Oct.	59.2	60.7
Markit flash services index	Oct.	58.2	54.9

This Week's Indicators

	Release Date	Period	Forecast*	Previous
Dallas Fed manufacturing survey	Mon.	Oct.	5.5	4.6
S&P CoreLogic Case-Shiller HPI (20-city, y/y)	Tues.	Aug.	19.8%	19.7%
Consumer confidence	Tues.	Oct.	109.0	109.3
New home sales	Tues.	Sept.	735,000	740,000
Richmond Fed manufacturing survey	Tues.	Oct.	-5	-3
Durable goods orders	Wed.	Sept.	0.3%	1.8%
Initial jobless claims	Thurs.	Week ending Oct. 23	280,000	290,000
Real GDP	Thurs.	Q3	1.9%	6.7%
GDP price index	Thurs.	Q3	6.9%	6.1%
Pending home sales	Thurs.	Sept.	3.3%	8.1%
KC Fed manufacturing survey	Thurs.	Oct.	19	22
Personal income	Fri.	Sept.	1.0%	0.2%
Personal consumption expenditures	Fri.	Sept.	0.6%	0.8%
Core PCE price index (m/m)	Fri.	Sept.	0.2%	0.3%
Core PCE price index (y/y)	Fri.	Sept.	3.7%	3.6%
Employment cost index	Fri.	Q3	0.8%	0.7%
Chicago PMI	Fri.	Oct.	63.8	64.7
Consumer sentiment	Fri.	Oct.	71.0	71.4

*** Nationwide Economics Forecast**

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