Popular Economics Weekly

WEEK OF MARCH 5, 2006—MARCH MADNESS

Spring is arriving with a bang. Mortgage applications surged as the season began early for home sales. This is while softness in the manufacturing sector with lower factory orders has put pressure on stocks. The flight to quality is lowering interest rates and therefore boosting mortgage activity.

Even the service sector showed a surprise drop in activity, according to the ISM, while the Federal Reserve's February Beige Book reported slower activity in 4 of its 12 districts. Rising labor costs and lower labor productivity in Q4 2006 could also be a sign of further inflationary pressures, as February's unemployment report showed fewer jobs created.

With interest rates falling, the number of mortgage applications as tracked by the Mortgage Bankers Association rose by 7.3% on a seasonally adjusted basis last week compared to the prior week, marking the highest total in two months.

And application volumes in the week ended March 2 were up about 16% compared with the same week a year ago, reported the MBA. The number of applications for loans to buy homes rose by 1 percent on a week-to-week basis and by about 2 percent compared to a year ago. Purchase loans have been relatively flat for six weeks, the MBA's data showed.

Meanwhile, applications for loans to refinance existing mortgages increased 15 percent from the week ended Feb. 23 to the highest level seen in 12 weeks. Refinancings were up about 38 percent compared with this time last year. Refinancings accounted for 46.1 percent of total applications filed last week, recovering after falling to a five-month low of 43.2 percent the week before.

UNEMPLOYMENT—Just 97,000 payroll jobs were created in February, including 39,000 government jobs. Construction lost another 62,000 jobs, a sign that the housing sector continues to slow. The jobless rate fell back to 4.5 percent, which was a statistical quirk, since the labor force shrank by 190,000. This is a sign of discouraged workers. A total of 374,000 workers dropped out of the workforce altogether.

FACTORY ORDERS—The surprise 6 point drop in the Institute for Supply Management's February activity index was in line with the 9 percent fall in durable goods' orders and 6 percent drop in all factory orders. The main culprit is lower auto sales, which are running a full 25 percent below last year, but so-called core capital equipment orders—equipment that producers need to produce more goods—also fell 6 percent. Those cutbacks mean that producers/factory owners see slower growth (and rising inventories) in the months ahead.

PRODUCTIVITY—A sure sign of a mature recovery (and maybe the reason for Alan Greenspan's remarks about the possibility of recession by year end) was the downward revision of fourth quarter labor productivity from 3 to a 1.6 percent increase in output per hour worked. This means workers required more hours to continue to produce more goods. But hourly wages are soaring, up 8 percent, meaning that industries have to compete for skilled workers.

CONSUMER CREDIT—Consumers' January credit card and installment loan borrowing increased just 3 percent, the slowest rate since last March. This could mean consumers are beginning to save more and spend less.

The mixed results of home sales, with January's existing-home sales increasing 3 percent, but new-home sales plunging 17 percent, does not yet a trend make. A 6 to 7-month supply of homes for sale means that prices and inventories probably have to fall further before we see a real recovery. Major builders are saying that new-home sales might not recover until 2008, at the earliest.

But some of the more affordable states are doing well. Ten states showed double digit home price increases in 2006, according to the Office of Housing Enterprise Oversight (OFHEO)—from Idaho's 17.55 percent to Mississippi's 9.6 percent increase. The national average price increase was 5.9 percent, slightly above the long-term average in personal incomes.