



May 2013 U.S. Economic & Housing Market Outlook

## Where's the Juice?

Has the economic recovery reached stall speed? Despite steady improvements in labor markets and a resurgent housing market, many fear the economic recovery is slowing down. Some may be wondering if the housing recovery is sustainable, if the lost construction jobs will come back, and if housing can once again drive the economy.

The juice for the economic recovery is going to come from housing, specifically new home construction, which will deliver the jobs to bring down the unemployment rate.

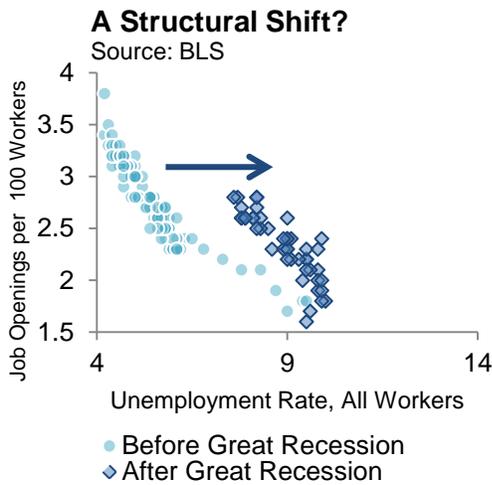
We expect that GDP growth in 2013 will be about 2 to 2.5 percent, well below its 3 to 3.5 percent potential. While the unemployment rate has been coming down, the reduction has not come from robust job growth; it has been the declining labor force participation rate driving the unemployment rate lower. As of April 2013, the percent of the population participating in the labor market was at 63 percent, lower than any time since 1980.



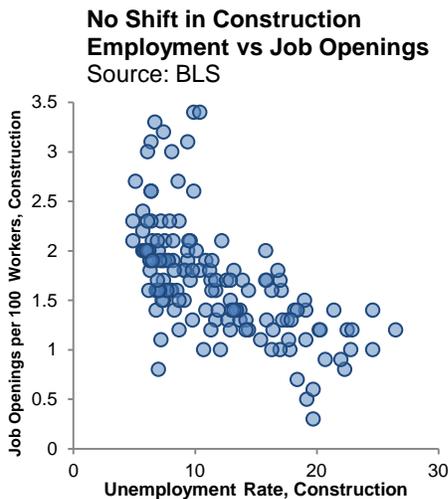
The declining participation rate and fall-off in the employment-to-population ratio tell a similar story about the slow recovery in jobs. For prime-age workers (aged 25 to 54), the percent employed averaged 80 percent in 2006 and 2007, but has averaged four percentage points less over the past twelve months. If the percent employed had returned to the 2006 and 2007 level, total employment would be 1.5 million higher today, and the unemployment rate about 1 percentage point lower. (Assuming today's participation rate if the new workers all came from outside the labor force, the unemployment rate would be reduced by 0.1 percentage points.)

The employment gain has also been weak when compared with past recoveries over the past 65 years. The recovery that started in June 2009 has been one of the slowest in U.S. history measured in terms of job growth. Most recoveries saw the economy add 2 million jobs (on an annual basis) within about a year of the end of the recession. Following the Great Recession it took 30 months for the economy to add 2 million jobs, the second worst only to the recovery that followed the 2001 recession.

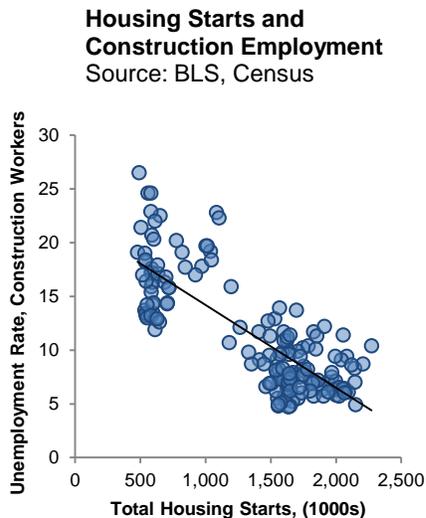
For these reasons the tough job market numbers have sparked fears that this time is different, and that the problems plaguing the labor market are structural. Essentially, the argument is that today's worker doesn't have the skills necessary in the current economy for the jobs that are available. Unlike cyclical unemployment, which can be cured by expansionary monetary or fiscal policy, structural unemployment is not easily undone. If the economy has really gone through a structural shift, then the persistent high unemployment and sluggish economic growth we have witnessed since the end of the Great Recession might be here to stay.



The broader labor market might have structural problems, but there is no sign of structural problems in the housing sector. The Bureau of Labor Statistic's JOLTS data provides valuable insights and rich information into labor market dynamics that are not available in the Household or Establishment Surveys. If we examine the April's JOLTS data together with unemployment rates, we can find a troubling sign. Since the Great Recession, the relationship between the unemployment rate and job openings appears to have shifted. Using historical averages before the Great Recession, with today's job openings the unemployment rate should be approximately 2 percentage points lower.



The relationship between the unemployment rate for construction workers and job openings has not shifted, as it apparently has for all other workers. The problem is structures, not structural. Construction is an extremely pro-cyclical industry and in this recovery not enough buildings are being built to put the millions of unemployed construction workers back to work. For every 1 percentage point increase in the unemployment rate for all workers, the unemployment rate for construction workers tends to increase by 2.5 percentage points. On average, construction workers have higher unemployment than other workers, but during an expansion, job gains in construction are typically substantial.



Based on historical correlations, every additional 100 thousand housing units started brings down the unemployment rate for construction workers by about three-fourths of a percentage point. We forecast that housing starts will increase by about 200,000 units in 2013, which would support over 100,000 new jobs in construction alone.

As new home construction ramps up, the unemployment rate will fall. With housing turning the corner cautious optimism has been on the rise. Home builders are anticipating improvements in the market over the next six months according to data released by the National Association of Home Builders. And the index gauging expectations for future sales edged up a single point in May to 53 – its highest level since February 2007.

At the start of the Great Recession the median time-on-market for new homes more than doubled, to over 14 months. Following the collapse in new home construction, the excess inventory of new homes for sale dropped, and the median time-on-market returned to historical norms. As of March, median time-on-market for new homes was 5 months, which is in line with historical averages. With near record low mortgage rates, relatively low for-sale inventory and increasing demand, time-on-market should continue to remain short in many parts of the country.

This confluence of events and market conditions will only result in even greater employment in the housing industry to keep up with the rising demand. Household formations are expected to gradually rise to a 1.2 to 1.4 million annual pace in coming years, supporting a sustained level of construction. Supplement this with replacement of existing stock and building for the second-home market housing starts should rise to 1.7 to 1.8 million dwellings by 2017. This will supply the juice to help strengthen the recovery.

Getting new home construction back in line with the fundamentals will do a lot to bring the economy back on track, and along with it, bring the unemployment rate down.

Frank E. Nothaft  
Chief Economist  
May 16, 2013

Leonard Kiefer  
Deputy Chief Economist

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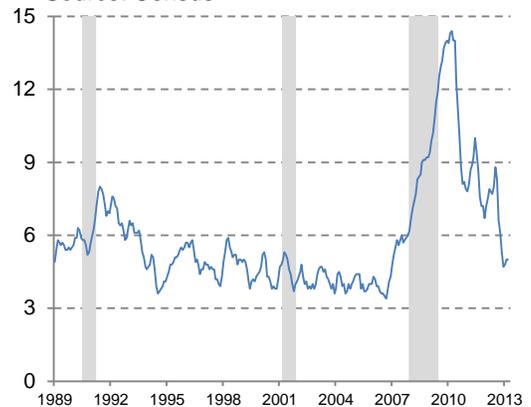
[chief\\_economist@freddiemac.com](mailto:chief_economist@freddiemac.com)

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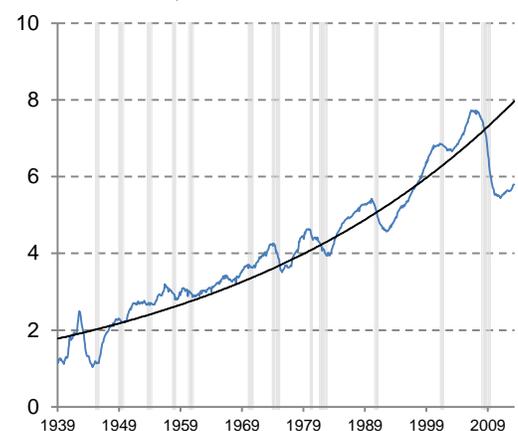
### Median Months on Market for New Homes

Source: Census



### Construction Employment

Millions SA, Source: BLS



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*Revised 5/16/2013*

Indicator	2012		2013				2014				Annual Totals					
	Q3	Q4	Q1	Q2	Q3	Q4	Q1	Q2	Q3	Q4	2009	2010	2011	2012	2013	2014
	Real GDP (%)	3.1	0.4	2.5	1.7	2.4	2.8	3.3	3.5	3.6	3.5	-0.1	2.4	2.0	1.7	2.4
Consumer Prices (%) a.	2.1	2.2	1.4	1.4	2.0	2.0	2.0	2.0	2.0	2.0	1.5	1.4	3.0	1.8	1.7	2.0
Unemployment Rate (%) b.	8.0	7.8	7.7	7.5	7.4	7.3	7.2	7.1	6.9	6.8	9.3	9.6	8.9	8.1	7.5	7.0
30-Year Fixed Mtg. Rate (%) b.	3.6	3.4	3.5	3.4	3.5	3.7	3.8	4.0	4.1	4.3	5.0	4.7	4.5	3.7	3.5	4.1
1-Year Treas. Indexed ARM Rate (%) b.	2.7	2.6	2.6	2.5	2.5	2.6	2.6	2.7	2.8	2.8	4.7	3.8	3.0	2.7	2.6	2.7
10-Year Const. Mat. Treas. Rate (%) b.	1.6	1.7	2.0	1.7	1.8	2.0	2.1	2.3	2.4	2.6	3.3	3.2	2.8	1.8	1.9	2.4
1-Year Const. Mat. Treas. Rate (%) b.	0.2	0.2	0.2	0.1	0.1	0.2	0.2	0.3	0.4	0.4	0.5	0.3	0.2	0.2	0.2	0.3

Indicator	2012		2013				2014				Annual Totals					
	Q3	Q4	Q1	Q2	Q3	Q4	Q1	Q2	Q3	Q4	2009	2010	2011	2012	2013	2014
	Housing Starts c.	0.78	0.90	0.96	0.98	1.00	1.05	1.10	1.15	1.25	1.30	0.55	0.59	0.61	0.78	1.00
Total Home Sales d.	5.11	5.28	5.36	5.45	5.50	5.65	5.75	5.95	6.10	6.20	4.72	4.51	4.57	5.03	5.49	6.00
FMHPI House Price Appreciation (%) e.	0.6	0.0	1.4	2.5	1.0	0.0	1.0	1.5	1.0	0.4	-2.3	-5.3	-3.6	6.0	5.0	3.5
S&P/Case-Shiller® Home Price Index (%) f.	2.1	-0.3	1.5	3.0	1.5	-1.0	0.5	2.0	0.7	0.3	-2.5	-3.8	-3.7	7.3	5.0	3.5
1-4 Family Mortgage Originations g.																
Conventional	\$453	\$425	\$398	\$430	\$340	\$285	\$280	\$340	\$245	\$185	\$1,549	\$1,300	\$1,208	\$1,627	\$1,453	\$1,050
FHA & VA	\$97	\$105	\$102	\$100	\$80	\$65	\$50	\$80	\$65	\$55	\$451	\$377	\$292	\$373	\$347	\$250
Total	\$550	\$530	\$500	\$530	\$420	\$350	\$330	\$420	\$310	\$240	\$2,000	\$1,677	\$1,500	\$2,000	\$1,800	\$1,300
ARM Share (%) h.	8	7	8	9	10	11	12	13	14	15	3	5	11	10	10	14
Refinancing Share - Applications (%) i.	82	83	79	70	65	60	60	50	45	40	70	76	75	81	69	50
Refinancing Share - Originations (%) j.	76	76	79	70	65	60	60	50	45	40	68	67	64	75	69	50
Residential Mortgage Debt (%) k.	-3.0	0.1	0.5	1.5	1.5	0.5	1.0	2.0	3.0	4.0	-1.6	-4.1	-2.2	-2.0	1.0	2.5

Note: Quarterly and annual forecasts (or estimates) are shown in shaded areas; totals may not add due to rounding; quarterly data expressed as annual rates.

Annual forecast data are averages of quarterly values; annual historical data are reported as Q4 over Q4.

a. Calculations based on quarterly average of monthly index levels; index levels based on the seasonally-adjusted, all-urban consumer price index.

b. Quarterly average of monthly unemployment rates (seasonally-adjusted); Quarterly average of monthly interest rates.

c. Millions of housing units; quarterly averages of monthly, seasonally-adjusted levels (reported at an annual rate).

d. Millions of housing units; total sales are the sum of new and existing single-family homes; quarterly averages of monthly, seasonally-adjusted levels (reported at an annual rate).

e. Quarterly growth rate of Freddie Mac's House Price Index (FMHPI); not seasonally-adjusted; Dec.to-Dec. for yearly data.

f. National composite index (quarterly growth rate); not seasonally-adjusted; Q4-to-Q4 for yearly data.

g. Billions of dollars (not seasonally-adjusted).

h. Federal Housing Finance Agency (FHFA); quarterly averages of monthly shares of number of loans of conventional, home-purchase mortgage closings (not seasonally-adjusted).

i. Primary Mortgage Market Survey®; quarterly averages of monthly shares of all single-family mortgage applications (not seasonally-adjusted).

j. Home Mortgage Disclosure Act for all single-family mortgages (not seasonally-adjusted); Annual share is dollar-weighted average of quarterly shares.

k. Federal Reserve Board; growth rate of residential mortgage debt, the sum of single-family and multifamily mortgages(not seasonally-adjusted, annual rate).

Prepared by Office of the Chief Economist and reflects views as of 5/16/2013 (MAS); Send comments and questions to chief\_economist@freddiemac.com.

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