



Ebbs and Flows

Economic recovery is rarely linear – different sectors of the economy gather momentum at different rates and some initially positive forces create drag at later times. For example, fiscal stimulus programs that gave the economy a boost in the latter half of 2009 and early part of 2010 will have lesser effect in the coming year. Some of those programs will continue for a bit longer and maintain economic activity at current levels (and therefore will not add to economic growth in coming quarters) while others will end, thus subtracting from aggregate demand. Similarly, hiring for the decennial census boosted the employment numbers temporarily, but in June most of those jobs had ended, reducing job growth. These facts and worries about spillovers from the fiscal crises in Europe and the Gulf oil disaster are leading some to proclaim that a double-dip recession is on the horizon. We see these as part of the normal pattern of ebbs and flows in recovery and believe that there is sufficient momentum to carry the U.S. economy forward, albeit moderately.

Importantly, business profits have turned around fairly quickly, rising in each of the last five quarters and it is here that the recovery has strong footing. Business profitability is now turning into investment in real capital goods and hiring of labor. Private, non-farm employment has risen every month since hitting a recession low in December 2009, adding nearly 600,000 jobs (seasonally adjusted) in total. In addition, already employed workers are working longer hours and their wages are also rising, giving a foundation on which consumer spending can grow. The Federal Reserve anticipates maintaining the current, exceptionally low level of its federal funds target for an extended period, and this accommodation will continue to support growth in the quarters ahead.

One reason why the recovery seems to have lost steam has been uncertainty over the Eurozone's economic vitality. While the economies of Germany and France appear to be recovering, there is heightened concern over the debt loads of some of the other nations in western and central Europe. The possibility of weaker economic growth in the Eurozone, coupled with depreciation in the Euro relative to the U.S. dollar, has reduced prospects of American exports to Europe as a propellant to the U.S. recovery.

In the housing market, the end of the homebuyer tax credits was expected to lead to a decline in home sales when the first stage of the program ended in April, which it did. The effect is clearest for new home sales, as this series reflects contract signings rather than settlements. New home sales for May fell 33 percent on a seasonally adjusted basis to 300,000 units (SAAR), the lowest since the Census Bureau's series began in 1963. In terms of existing home sales, which reflect settlements rather than contract signings, the surge in sales was more moderate than the jump in new home sales at just under 10 percent, and existing home sales slipped by only 2 percent in May. Thus, the homebuyer tax credit programs were successful in promoting demand for home purchases and accelerated the timing of the home-purchase decision for many first-time buyers and some repeat buyers, leading to an initial decline in



purchase contracts immediately after the expiration of the credits. In coming months we will learn how strong demand is for home purchases without the tax credits; low mortgage rates, more affordable home prices and an improving jobs outlook should keep the trend in sales generally headed upwards toward year end and into 2011.

Interest rates on 30-year and 15-year fixed-rate conventional conforming loans have fallen steadily since April, setting record lows in the weeks ended June 24, July 1 and July 8, respectively, as measured by Freddie Mac's Primary Mortgage Market Survey®; the survey began capturing 30-year fixed-rate data in April 1971. Data from other, pre-1971 surveys indicate that these are the lowest mortgage interest rates in more than one-half century and should help promote homebuyer affordability – the decline in rates of half a percentage point over the past two months means that a family that buys the average priced home will have a mortgage payment about \$70 lower than a family that purchased that same home in April.

The news on home prices has been mixed across various indices in recent months, with some up and some down, but the downs are smaller and the ups more prevalent than they were three months ago. CoreLogic's single-family combined house-price index indicates that as of May, nine states saw declines of more than 2.5 percent over the previous 12 months and 17 states saw increases of at least 2.5 percent. In February, these numbers were 14 and eight, respectively. When distressed properties (REO sales) were removed, the pattern remains the same, but numbers change to six states seeing annual declines of more than 2.5 percent as of May (versus 20 in February) and seven states with increases of 2.5 percent or more (versus three in February).

Despite some signs of stabilization, delinquency rates on single-family and multifamily loans remain high. The Mortgage Bankers Association reported that serious delinquency rates on single-family loans dipped to 9.5 percent as of March 31, down from year-end 2009 but still the second highest rate in the 50-year history of their survey. The noncurrent rate on multifamily loans at FDIC-insured institutions rose to 4.6 percent as of March 31, the highest since 1992; the Federal Reserve Board's April Survey of Bank Lending Practices reported a sizable fraction of banks reported having increased their use of commercial real estate loan extensions over the previous six months. Residential loan performance was better in areas with lower unemployment rates and where property prices have fallen little, if at all. The gradual employment recovery and stabilization in home prices should lead to lower delinquency rates for the overall market by 2011. It will be a while still until the housing market is robust again, but like the macroeconomy, small improvements are already occurring, and we believe the momentum will carry through the occasional setbacks.

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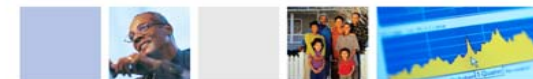
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July 2010 Economic and Housing Market Outlook



Office of the Chief Economist

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Major Economic Indicators

Indicator	2009				2010				2011				Annual Totals					
	Q1	Q2	Q3	Q4	Q1	Q2	Q3	Q4	Q1	Q2	Q3	Q4	2007	2008	2009	2010	2011	2012
Real GDP (%)	-6.4	-0.7	2.2	5.6	2.7	3.5	3.0	3.3	3.5	3.5	3.5	3.5	2.5	-1.9	0.1	3.1	3.5	3.5
Consumer Prices (%) a.	-2.2	1.9	3.7	2.6	1.5	-0.4	1.5	1.5	1.5	1.5	1.5	1.5	4.0	1.6	1.5	1.0	1.5	2.5
Unemployment Rate (%) b.	8.1	9.3	9.6	10.0	9.7	9.7	9.6	9.3	9.1	8.9	8.7	8.5	4.6	5.8	9.3	9.6	8.8	8.0
30-Year Fixed Mtg. Rate (%) b.	5.1	5.0	5.2	4.9	5.0	4.9	4.7	4.8	5.0	5.2	5.3	5.5	6.3	6.0	5.0	4.8	5.2	5.9
1-Year Treas. Indexed ARM Rate (%) b.	4.9	4.8	4.7	4.4	4.3	4.0	4.0	4.0	4.1	4.2	4.3	4.5	5.6	5.2	4.7	4.1	4.3	4.9
10-Year Const. Mat. Treas. Rate (%) b.	2.7	3.7	3.5	3.5	3.7	3.5	3.1	3.2	3.4	3.6	3.7	3.9	4.6	3.7	3.3	3.4	3.7	4.3
1-Year Const. Mat. Treas. Rate (%) b.	0.6	0.5	0.5	0.4	0.4	0.4	0.3	0.3	0.4	0.5	0.6	0.7	4.5	1.8	0.5	0.4	0.6	1.0

Housing and Mortgage Markets

Indicator	2009				2010				2011				Annual Totals					
	Q1	Q2	Q3	Q4	Q1	Q2	Q3	Q4	Q1	Q2	Q3	Q4	2007	2008	2009	2010	2011	2012
Housing Starts c.	0.53	0.54	0.59	0.57	0.62	0.63	0.68	0.73	0.85	0.95	1.05	1.15	1.36	0.91	0.55	0.66	1.00	1.50
Total Home Sales d.	4.47	4.62	5.05	5.61	4.86	5.40	4.80	5.00	5.40	5.80	6.00	6.20	5.72	4.84	4.94	5.02	5.85	6.60
Conventional Mtg. Home Price Index (%) e.	4.6	-9.9	-8.2	-2.5	-6.0	-1.5	-1.5	0.0	0.0	1.0	1.5	1.5	-0.3	-5.5	-4.2	-2.3	1.0	2.0
S&P/Case-Shiller® Home Price Index (%) f.	-26.2	13.0	13.9	-4.1	-12.3	2.0	2.0	-1.0	0.0	0.5	1.5	2.0	-8.4	-18.3	-2.3	-2.3	1.0	4.0
1-4 Family Mortgage Originations g.																		
Conventional	\$354	\$458	\$398	\$339	\$250	\$255	\$269	\$248	\$250	\$263	\$272	\$265	\$2,312	\$1,310	\$1,549	\$1,022	\$1,050	\$1,300
FHA & VA	\$96	\$125	\$119	\$111	\$92	\$89	\$100	\$97	\$80	\$90	\$90	\$90	\$120	\$290	\$451	\$378	\$350	\$300
Total	\$450	\$583	\$517	\$450	\$342	\$344	\$369	\$345	\$330	\$353	\$362	\$355	\$2,432	\$1,600	\$2,000	\$1,400	\$1,400	\$1,600
ARM Share (%) h.	1	3	4	5	4	4	5	6	7	8	9	10	10	7	3	5	9	12
Refinancing Share - Applications (%) i.	78	70	59	74	70	65	60	50	35	35	35	35	42	48	70	61	35	35
Refinancing Share - Originations (%) j.	75	69	61	77	73	69	64	55	40	40	40	40	49	50	70	65	40	40
Residential Mortgage Debt (%) k.	-0.3	-1.3	-2.8	-2.4	-3.6	-2.0	-1.0	0.0	2.0	4.0	2.0	4.0	7.1	-0.4	-1.7	-1.7	3.0	6.0

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 (not seasonally-adjusted).
- 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 detached single-family homes; quarterly averages of monthly, seasonally-adjusted levels (reported at an annual rate).
- e. Annualized growth rate of Freddie Mac's Conventional Mortgage Home Price Index (CMHPI); not seasonally-adjusted
- f. National composite index (annualized growth rate), not seasonally-adjusted
- g. Billions of dollars (not seasonally-adjusted).
- h. Federal Housing Finance Board (FHFB); quarterly averages of monthly shares 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 7/12/2010 (MAS); Send comments and questions to chief_economist@freddiemac.com.

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