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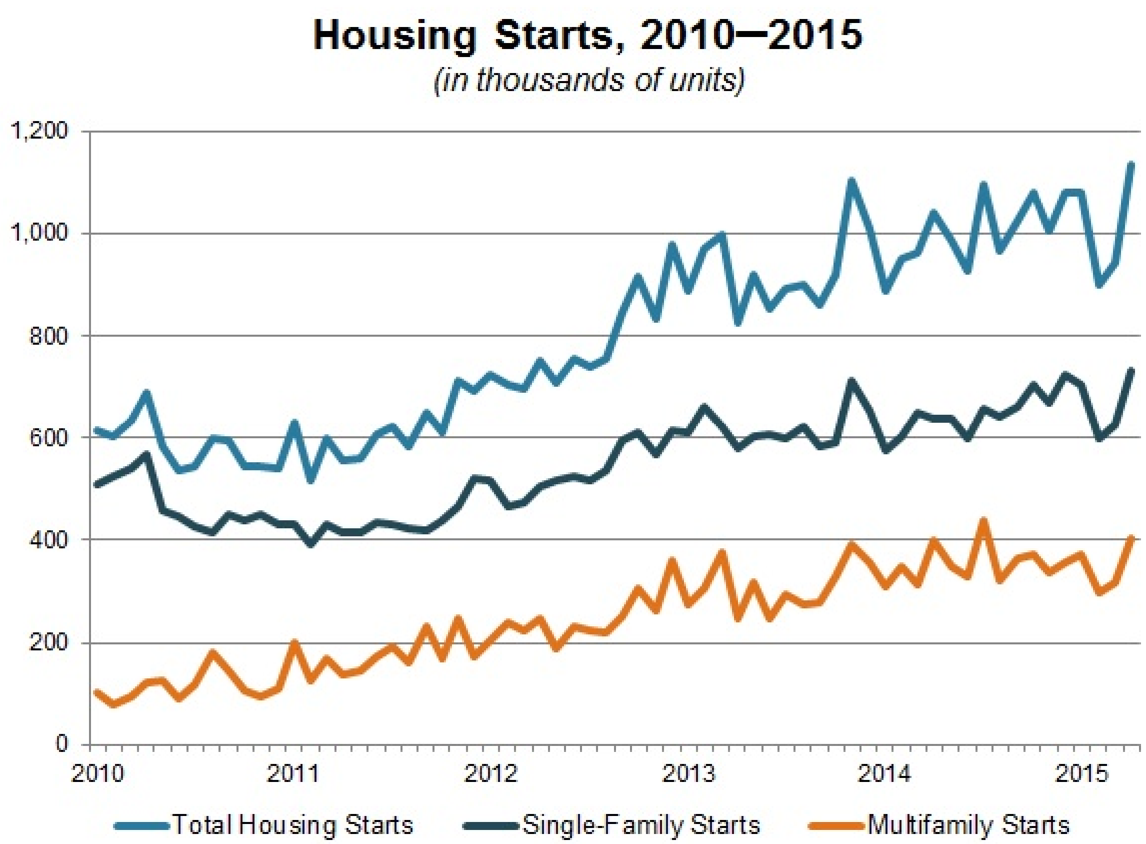

The minutes of the April 28–29 Federal Open Market Committee (FOMC) meeting highlighted the nuance that many of us see in the economy right now. The Federal Reserve highlighted a number of challenges facing consumers and businesses in the early months of 2015, noting how these headwinds have dampened overall activity year-to-date. On the other hand, the FOMC felt that slowing economic growth was largely due to "transitory factors," with its outlook mostly unchanged for the rest of this year. The Federal Reserve projects growth of 2.3 to 2.7 percent in 2015, and it expects the unemployment rate to fall to 5.0 to 5.2 percent.

Despite this cautious optimism for a rebound in the economy, the main headline coming out in these minutes was the possible timing of increasing short-term interest rates. The Federal Reserve had been operating on automatic pilot in its pursuit of normalized policies, with quantitative easing ending in October 2014 and the

FOMC on a path toward raising the federal funds rate at its June 16–17 meeting. Yet, weaker-than-desired data of late have caused participants to question the June timing, with conventional wisdom now suggesting that short-term rates are likely to go up at the September 16–17 meeting instead. The FOMC meeting minutes seem to confirm this, stating the following:

> *Although participants expressed different views about the likely timing and pace of policy firming, they agreed that the Committee's decision to begin firming would appropriately depend on the incoming data and their implications for the economic outlook. A few anticipated that the information that would accrue by the time of the June meeting would likely indicate sufficient improvement in the economic outlook to lead the Committee to judge that its conditions for beginning policy firming had been met. Many participants, however, thought it unlikely that the data available in June would provide sufficient confirmation that the conditions for raising the target range for the federal funds rate had been satisfied, although they generally did not rule out this possibility.*

For those looking for a rebound in manufacturing activity, we have not seen one yet. Surveys released last week from Markit and the Kansas City and Philadelphia Federal Reserve Banks continued to reflect softness in the sector. The Kansas City report was the weakest, with its composite index contracting for the third straight month. In contrast, the other two releases noted expanding levels of new orders, production and employment, albeit with some easing for the month. While exports are expected to remain weak moving forward, respondents to these surveys are hopeful that demand, output, hiring and capital spending will pick up in the coming months.

Meanwhile, manufacturing activity in the Eurozone improved to its highest level since April 2014, and Japan's economy also continues to edge higher. Yet, the HSBC Flash China Manufacturing PMI has now contracted in five of the past six months, reflecting decelerated growth. (For more information on these trends, see the most recent Global Manufacturing Economic Update.)

There was more encouraging news on the housing front. New housing starts jumped from an annualized 944,000 in March to 1,135,000 in April, its fastest pace since November 2007, the month before the start of the Great Recession. As such, it appears that the housing market has begun to move past the weather-related softness seen in some regions of the country in February and March. On a year-over-year basis, housing starts have risen 9.2 percent since April 2014. The housing permits data were equally reassuring. Housing permits increased from 1,038,000 units at the annual rate to 1,143,000, hitting its highest level since June 2008. In other news, homebuilder confidence ebbed slightly in May but remained positive overall. Existing home sales declined in April; yet, reduced supplies of homes for sale have pushed prices higher.

On Friday of this week, the Bureau of Economic Analysis will issue a revision to first quarter real GDP, which is expected to fall slightly into negative territory after originally being estimated as a 0.2 percent increase. We also will see several indicators on the health of the manufacturing sector on Tuesday, including April durable goods orders and shipments and May sentiment surveys from the Dallas and Richmond Federal Reserve Banks. Other highlights next week include the latest data on consumer confidence, new home sales and state employment.

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Economic Indicators

Last Week's Indicators:
(Summaries Appear Below)

Monday, May 18
NAHB Housing Market Index

Tuesday, May 19
Housing Starts and Permits

Wednesday, May 20
None

Thursday, May 21
Conference Board Leading Indicators
Existing Home Sales
Kansas City Fed Manufacturing Survey
Markit Flash PMIs for the United States, Eurozone and China
Philadelphia Fed Manufacturing Survey

Friday, May 22
Consumer Price Index

This Week's Indicators:

Monday, May 25
MEMORIAL DAY HOLIDAY

Tuesday, May 26
Conference Board Consumer Confidence
Dallas Fed Manufacturing Survey
Durable Goods Orders and Shipments
New Home Sales
Richmond Fed Manufacturing Survey

Wednesday, May 27
State Employment Report

Thursday, May 28
None

Friday, May 29
Gross Domestic Product (Revision)
University of Michigan Consumer Sentiment (Revision)

Summaries for Last Week`s Economic Indicators

Conference Board Leading Indicators

According to the Conference Board, the Leading Economic Index (LEI) rose 0.7 percent in April, building on the 0.4 percent gain observed in March. As such, these data point to a rebound in economic activity in the coming months, with the LEI up 4.0 percent at the annual rate over the past six months. April's increase stemmed largely from non-manufacturing components, including building permits *(see below)*, consumer confidence, favorable credit conditions, the interest rate spread, the stock market and unemployment claims. Yet, softness in manufacturing activity, particularly new orders and the average workweek, dragged down the LEI.

Similarly, industrial production pulled the Coincident Economic Index (CEI) lower, subtracting 0.04 percentage points from the headline figure. Nonetheless, the CEI increased 0.2 percent in April due to positive contributions from the other components. These included nonfarm payrolls, personal income and manufacturing and trade sales.

Consumer Price Index

The Bureau of Labor Statistics reported that consumer prices rose 0.1 percent in April, slightly lower than the 0.2 percent gains observed in both February and March. Lower energy prices helped to reduce the pace of the headline number, with energy costs down 1.3 percent for the month. Gasoline prices declined 1.9 percent in April, easing a bit after 2.4 percent and 3.9 percent increases observed in February and March, respectively. On a year-over-year basis, gasoline sells for 31.7 percent less today than in April 2014. Note that the average price of gasoline has risen a little since then, with the Energy Information Administration reporting that the average price of regular gasoline was $2.604 per gallon on May 18, up from $2.315 on April 6. This is still more than one dollar lower than 12 months ago.

Meanwhile, food costs were unchanged in April, with prices of food for the home down 0.2 percent and food outside the home up 0.2 percent. The costs of fruits and vegetables increased 0.2 percent, but other prices were largely lower, including for cereals and bakery products, dairy products and meats. Food costs have risen 2.0 percent year-over-year, with food prices decelerating over the past few months, down from 3.4 percent year-over-year in December. Moving forward, we would expect to see higher costs for eggs, with bird flu decimating supply.

Overall, the consumer price index has declined 0.1 percent over the past 12 months, with reduced energy costs pushing the headline figure lower year-over-year. Core inflation, which excludes food and energy prices, has risen 1.8 percent year-over-year in April, the same pace as in March. It has remained below 2 percent since February 2013, or 26 straight months. In April, costs were higher for medical care, new vehicles, shelter and transportation services, but these increases were offset somewhat by declining prices for apparel, household furnishings and used cars and trucks.

Existing Home Sales

The National Association of Realtors® (NAR) reported a decline in existing home sales, from an annualized 5.21 million units in March to 5.04 million in April. Only the Midwest saw increased sales in April, with the South experiencing the steepest declines. In particular, single-family homes weakened the most, with multifamily units remaining largely unchanged. Interestingly, the decrease occurred at a time when inventories fell dramatically. As Lawrence Yun, NAR's chief economist, stated, "April's setback is the result of lagging supply relative to demand and the upward pressure it's putting on prices."

The number of months of supply on the market rose sharply from 4.6 months in March to 5.3 months in April, illustrating the drop in inventories. The median sales prices for existing homes reached $219,400, an 8.9 percent increase from one year ago.

Housing Starts and Permits

According to the Census Bureau and the U.S. Department of Housing and Urban Development, residential construction activity rebounded strongly in April. New housing starts jumped from an annualized 944,000 in March to 1,135,000 in April, its fastest pace since November 2007, the month before the start of the Great Recession. As such, it appears that the housing market has begun to move past the weather-related softness seen in some regions of the country in February and March. On a year-over-year basis, housing starts have risen 9.2 percent since April 2014.

Both single-family (up from 628,000 to 733,000) and multifamily (up from 316,000 to 402,000) housing starts climbed in April, which was encouraging. The single-family growth rate marks the fastest since January 2008, with multifamily starts reaching a nine-month high.

The housing permits data were equally reassuring. Housing permits increased from 1,038,000 units at the annual rate to 1,143,000, hitting its highest level since June 2008. Single-family permitting rose from 642,000 to 666,000 for the month, whereas permits for multifamily units increased from 396,000 to 477,000.

Kansas City Fed Manufacturing Survey

The Kansas City Federal Reserve Bank reported that manufacturing activity contracted for the third consecutive month in May. The composite index dropped from -7 in April to -13 in May, suggesting a sharper drop in activity than the month before. Indeed, several of the key data points declined at faster rates in May than in April. This included new orders (down from -12 to -19), production (down from -2 to -13), shipments (down from -7 to -9) and the average workweek (down from -10 to -14). At the same time, employment (up from -18 to -17) continued to decrease sharply, and exports (up from -12 to -9) contracted for the fifth straight month, even as both measures fell at slightly slower paces.

The sample comments suggest that challenges in the larger economy are weighing heavily on the minds of survey respondents. Indeed, manufacturers noted the low price of crude oil, the strong U.S. dollar, the cost and complexity of government regulations and the weakened outlook as challenges. One respondent cited difficulty in finding qualified candidates to hire.

These headwinds have dampened the forward-looking outlook in the Kansas City district. The future-oriented composite index dropped from 6 to 0, its lowest level since July 2009. The underlying data reflect a decelerated expectation of new orders (down from 21 to 2), production (down from 17 to 6), shipments (down from 16 to 12) and capital spending (down from 10 to 0) over the next six months. Exports (up from -6 to -2) were anticipated to shrink once again, as was the average employee workweek (down from -5 to -13). On the positive side, at least one-quarter of those taking the survey still expect sales, production, shipments and hiring to increase over the coming months.

Markit Flash PMIs for the United States, Eurozone and China

The Markit Flash U.S. Manufacturing PMI declined from 54.1 in April to 53.8 in May, easing to its lowest level since October 2013, falling for the second straight month. The deceleration in May reflected slower growth in new orders (down from 55.3 to 54.2) and output (down from 55.3 to 55.0). Exports (up from 48.8 to 49.6) continued to contract, but declined by less for the month. On the positive side, hiring (up from 53.7 to 54.3) accelerated to its fastest rate in six months. Moreover, even with some weakening in sentiment, the measures for demand and production growth for manufacturers in the United States remains decent overall.

Meanwhile, the Markit Flash Eurozone Manufacturing PMI increased from 52.0 to 52.3, its highest level since April 2014. New orders (up from 51.8 to 52.6), output (up from 53.4 to 53.5) and exports (up from 52.3 to 53.0) each expanded modestly in May, with hiring growth (unchanged at 51.9) holding steady at nearly a four-year high. Overall, the economy today in Europe is better than it has been in a while, and yet, strong growth remains elusive. Real GDP rose 0.4 percent in the first quarter, edging up from 0.3 percent growth in the fourth quarter. On a year-over-year basis, the Eurozone grew 1.0 percent. The good news, however, is that the data points continue to move in the right direction, which is encouraging.

At the same time, Japan's economy improved somewhat in May. The Markit Flash Japan Manufacturing PMI rose from 49.9 to 50.9, a three-month high. Stronger new orders (up from 48.8 to 51.2) and output (up from 49.3 to 51.7) helped to buoy the headline number, with each rebounding after contracting the month before. In addition, exports (up from 50.3 to 50.5) and hiring (up from 50.4 to 51.1) both accelerated a little in May. Along those lines, Japanese real GDP grew 0.6 percent in the first quarter, strengthening from the 0.3 percent increase in the fourth quarter and declines in second and third quarters of 2014.

In contrast to other markets, the HSBC Flash China Manufacturing PMI declined at a slightly slower pace, up from 48.9 in April to 49.1 in May. It has contracted in five of the past six months, reflecting a decelerated rate of growth in China. The underlying May data suggested that activity contracted across the board, but at varying degrees. New orders (up from 48.7 to 49.3) and employment (up from 47.8 to 49.0) decreased by less, whereas output (down from 50.0 to 48.4) and exports (down from 50.3 to 46.8) both fell into negative territory for the month. The decline in production marks the fastest since April 2014. As such, these data reflect the easing in growth noted in the most recent Global Manufacturing Economic Update, including output from manufacturers, retail sales and fixed investments.

Final data points for all of these measures will come out on Monday, June 1.

NAHB Housing Market Index

The Housing Market Index (HMI) fell from 56 in April to 54 in May, according to the National Association of Home Builders (NAHB) and Wells Fargo. As such, sentiment among homebuilders remained somewhat nuanced. There has been a slight pullback in optimism since the end of last year, with the HMI measuring 58 in December. Still, the good news is that builders remain more upbeat than not, with the HMI exceeding 50 for 11 straight months. Values of more than 50 indicate that more homebuilders have positive outlooks than negative.

Only the Midwest region experienced some easing in the HMI in May, with sentiment in the West edging marginally higher and indices in the Northeast and South holding steady. Looking at single-family sales activity, the data were mixed. Current sales slightly decelerated, with the index dropping from 61 to 59. Yet, homebuilders were more enthusiastic in their assessments of sales over the next six months (up from 63 to 64) than they have been in five months.

Philadelphia Fed Manufacturing Survey
The Philadelphia Federal Reserve Bank reported that the manufacturing outlook eased slightly in May. The composite index of general business activity dropped from 7.5 in April to 6.7 in May. In general, the outlook has weakened so far this year relative to last year, with the headline measure averaging 6.1 through the first five months of 2015. This compares to the more-robust average of 25.1 in the second half of 2014, with the softness experienced year-to-date largely the result of a number of headwinds seen in the U.S. and global economies. At the same time, manufacturers in the district have reported expanding levels of activity for 15 straight months.

Despite the easing in the composite index, the data showed some encouraging signs. Both new orders (up from 0.7 to 4.0) and shipments (up from -1.8 to 1.0) improved, and pricing pressures (down from -7.5 to -14.2) continued to decline, mostly because of reduced energy costs. At the same time, hiring (down from 11.5 to 6.7) slowed somewhat, and the average employee workweek (down from 3.4 to -5.6) narrowed.

The good news is that manufacturers continue to be mostly upbeat moving forward. Roughly 45 percent of respondents to the survey anticipate increased orders and shipments over the next six months. In addition, 51.3 percent expect to hire additional workers over the next year, with 34.2 percent noting difficulty in being able to fill vacancies and 22.1 percent reporting difficulty in retaining existing employees. This suggests that manufacturers are planning to hire more as a result of expecting better demand and production in the coming months—a finding confirmed by increases in planned capital expenditures (up from 15.8 to 16.8).

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Questions or comments?

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