THE AUSTIN ADVISOR

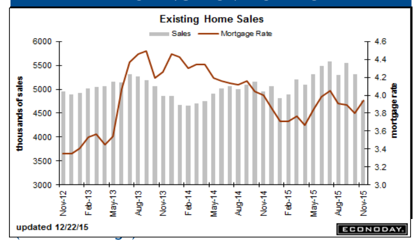
January 18, 2016

Markets	11-Jan	12-Jan	13-Jan	14-Jan	15-Jan	YTD%	31-Dec-15
DJIA	16,398.57	16,516.22	16,151.41	16,379.05	15,988.08	-8.25%	17,425.03
S&P 500	1,923.67	1,938.68	1,890.28	1,921.84	1,880.33	-8.00%	2,043.94
NASDAQ	4,637.99	4,685.92	4,526.06	4,615.00	4,488.42	-10.36%	5,007.41
SNL Bank Index	393.78	396.99	384.14	388.67	377.11	-12.60%	431.48
Fed Funds Rate	0.36%	0.36%	0.36%	0.36%	0.36%		0.35%
1 Month LIBOR	0.42%	0.42%	0.43%	0.43%	0.43%		0.43%
3 Month LIBOR	0.62%	0.62%	0.62%	0.62%	0.62%		0.61%
3 Month T-Bill	0.21%	0.21%	0.22%	0.25%	0.24%		0.16%
1 Year Treasury	0.63%	0.62%	0.60%	0.55%	0.49%		0.65%
2 Year Treasury	0.94%	0.93%	0.91%	0.90%	0.85%		1.06%
3 Year Treasury	1.20%	1.18%	1.15%	1.14%	1.08%		1.31%
5 Year Treasury	1.58%	1.55%	1.51%	1.52%	1.46%		1.76%
10 Year Treasury	2.17%	2.12%	2.08%	2.10%	2.03%		2.27%
30 Year Treasury	2.96%	2.89%	2.85%	2.90%	2.81%		3.01%

WEEKLY HIGHLIGHT

Equity market pricing reflects the fear that problems in China will spread to the U.S.

EXISTING HOME SALES



Economy		Week of January 11, 2016
JOLTS Index	5.431 Million	This index of unfilled job openings is running at record high levels, and increased in November with job growth to follow
Producer Price Index	-0.2%	Down in December after rising 0.3% in November, with the core rate up 0.1% to close out the year
Retail Sales	-0.1%	The headline data was less than expected, but this is not an inflation adjusted data report
Industrial Production	-0.4%	The topline number was less than expected, while excluding utility output manufacturing was down 0.1%
Capacity Utilization	76.5%	The operating rate dropped from 76.9%, reflecting a weak manufacturing sector as the dollar keeps exports low

MONDAY MUSING

If you have never been to the Upper Peninsula of Michigan in the winter, you may not believe this newspaper story from last week. I can tell you first hand there are only four things to do in the winter for upper's. They can snowmobile, ice fish, or drink. The fourth activity you can figure out for yourself. At any rate, the story was about four guys engaged in drinking when they decided to go ice fishing. They were arrested an hour later but not for public intoxication. They were arrested for vandalism when they were caught cutting a hole in the ice at the public indoor skating rink. The lesson is never combine two activities at one time when one of them is drinking.

Calendar	Release	Covering	Week of January 18, 2016
Consumer Price Index	Tuesday	December	The consensus forecast calls for no change and up 0.2% for the core rate, with low gas prices yet to affect the data
Housing Starts	Tuesday	December	Starts have been volatile, but are expected to be strong at 1.21 million, up from 1.173M in November
Existing Home Sales	Friday	December	Sales are expected to recover from the weak November data due to regulation changes; at 5.21 Million, up from 4.769M
Leading Indicators	Friday	December	This index has been trending to a lower level with forecasts of unchanged in December after being +0.4% in November

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Commentary

The financial world has changed. We cannot look to past market cycles to guide us in this environment. **Stock prices** are being driven by traders, derivatives, short-term investors and massive flows of capital moving at the click of a button. Short-term price movements have little to do with long-term fundamentals. In the last two weeks, investors have decided the drop in commodity prices and the slowing growth in **China** is going to drag economic growth down globally. They have followed each other to the door, and tried to get out of stocks. That capital has flowed into the **bond market**. The magnitude of the move is exacerbated by instant trading decisions based on data from a country like China, that does not have the liquidity in their markets to manage these large capital outflows. Their response was to de-value their currency, which only served to magnify the downside volatility. The question is whether this market downturn will cause a loss of confidence in the U.S. and really lead us into a recession. The concern is there was an asset **pricing bubble** in stocks and commercial real estate driven by low **interest rates** in the past seven years.

The drop in stock prices could cause **consumer spending** to slow if **confidence** is affected. Consumer spending has been driving an acceleration in economic growth, as the economy transitioned from the manufacturing led recovery out of the Great Recession. This spending was fueled by **job growth** and the beginning of better growth in wages from a tight **labor market**. This was confirmed last week, with the **JOLTS index** up again in November. That indicates job growth will remain strong in the next several months. The drop in **retail sales** for December is misleading. Retail sales are measured in dollar terms, but not adjusted for **inflation**. When gas prices decline, retail sales will be lower, even if the number of gallons of gas purchased goes up. Additionally, retail sales is seasonally adjusted but the adjustment does not fully reflect the changes in the nature of spending for the holidays. For example, gift cards are not counted as sales until they are used, rather than when they are purchased. This shifts sales into the early part of the this year. This factor is getting more important as the use of gift cards has increased by large amounts in the past several years.

Personal consumption expenditures included in the **Real GDP** data adjusts for price changes and measures unit volume. The **housing data** due out this week is expected to be solid, with December **home sales** recovering from the drop in November, due to changes in documentation requirements to close a mortgage. In short, the data does not support the drop in equity prices experienced this year. Investors are discounting a change in the current environment. Only time will tell whether this is appropriate. Our forecast has not changed as of yet as we believe strong job growth in a service based economy and faster income growth will keep our economy on track.

Trusted Advisor to Financial Institutions
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