THE PROBANK AUSTIN ADVISOR

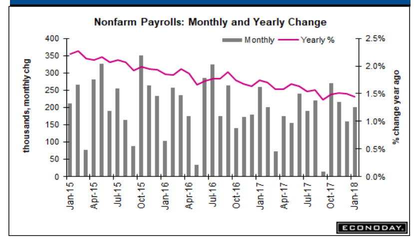
March 5, 2018

Markets	26-Feb	27-Feb	28-Feb	1-Mar	2-Mar	YTD%	29-Dec-17
DJIA	25,709.27	25,410.03	25,029.20	24,608.98	24,538.06	-0.73%	24,719.22
S&P 500	2,779.60	2,744.28	2,713.83	2,677.67	2,691.25	0.66%	2,673.61
NASDAQ	7,421.46	7,330.36	7,273.01	7,180.56	7,257.87	5.13%	6,903.39
SNL Bank Index	657.53	650.09	641.61	632.90	636.48	3.04%	617.68
Fed Funds Rate	1.42%	1.42%	1.35%	1.42%	1.42%		1.42%
1 Month LIBOR	1.65%	1.66%	1.67%	1.69%	1.69%		1.56%
3 Month LIBOR	1.98%	2.01%	2.02%	2.02%	2.03%		1.69%
3 Month T-Bill	1.66%	1.66%	1.65%	1.63%	1.65%		1.39%
1 Year Treasury	2.03%	2.08%	2.07%	2.05%	2.06%		1.76%
2 Year Treasury	2.22%	2.27%	2.25%	2.22%	2.25%		1.89%
3 Year Treasury	2.37%	2.43%	2.42%	2.36%	2.40%		1.98%
5 Year Treasury	2.60%	2.67%	2.65%	2.58%	2.63%		2.20%
10 Year Treasury	2.86%	2.90%	2.87%	2.81%	2.86%		2.40%
30 Year Treasury	3.15%	3.17%	3.13%	3.09%	3.14%		2.74%

WEEKLY HIGHLIGHT

We added a new risk to inflation last week with the possibility of trade wars

UNEMPLOYMENT RATE



(click to enlarge)

Economy	Week of February 26, 2018	
New Home Sales	593,000	Well below expectations and offsets the strong data from the last two months leaving, Y/Y at down 1%
Durable Goods Orders	-3.7%	Another weaker than expected report but Y/Y is 6.8% and excluding the volatile transportation sector, growth is 6.9%
Consumer Confidence	130.8	In spite of financial market volatility, confidence rose from a revised 124.3 led by the outlook for jobs
Real GDP-Revised	2.5%	Growth in the fourth quarter was only changed by 0.1% down from 2.5% with the trade deficit and low inventory growth still the issue
Motor Vehicle Sales	17.1 Million	The issue of strong confidence and income growth not driving consumption higher was the report for January
Personal Income	0.4%	This is above the monthly average of the last year providing further evidence of rising inflationary pressures
Personal Spending	0.2%	The issue of strong confidence and income growth not driving consumption higher was the report for January
Core PCE Price Index	0.3%	This is above the monthly average of the last year providing further evidence of rising inflationary pressures
ISM Index	60.8	This is a 14 year high for the index that has the best record of telling us where manufacturing activity is headed

ON THIS DAY IN HISTORY

1770 - Civilians and soldiers clash in the Boston Massacre

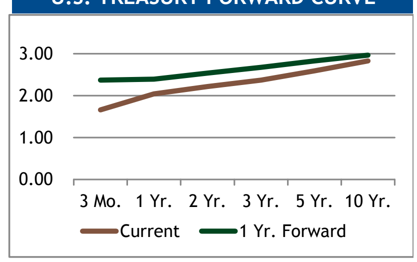
1946 - British Prime Minister, Winston Churchill, delivers Iron Curtain speech

1953 - Joseph Stalin, leader of the Soviet Union, dies in Moscow

1993 - Boston Celtic, Larry Bird, undergoes backfusion surgery

Calendar	Release	Covering	Week of March 5, 2018
Trade Deficit	Wednesday	January	No narrowing of the trade deficit is expected in spite of stronger foreign economies and a weaker dollar
Consumer Credit	Wednesday	January	Credit growth of $18 billion is expected with credit card balances growth of 6% continuing to boost totals
Unemployment Rate	Friday	February	Further evidence of a tight labor market is expected with the unemployment rate dropping to 4.0% from 4.1%
Nonfarm Payrolls	Friday	February	Job growth is expected to remain strong with 205,000 expected or about the same as January which was +200,000
Avg. Hourly Earnings	Friday	February	Inflation risks started with wage growth accelerating but some moderation is expected at just 0.2% expected

U.S. TREASURY FORWARD CURVE



THE PROBANK AUSTIN ADVISOR

Commentary

As if we did not have enough risk affecting **financial markets**, we added the possibility of **trade wars** last week. Discussion of imposing tariffs on certain **imported goods** could lead to retaliation by our trading partners and disrupting the **flow of goods** and services. The largest drag on **U.S. economic growth** in the past two years is the large increase in the **trade deficit**. Much of the growth in consumption is being met with imports. We have expected the trade deficit to narrow as growth in **foreign markets** has improved and the dollar has declined. A **lower dollar** relative to other currencies would make our products and services less expensive in these growing foreign markets and make their goods more expensive in our market. We would become more **price-competitive** with a lower dollar. To date, this has not happened with the trade deficit remaining at an elevated level relative to historical averages. The decline in the dollar has occurred over a short period of time beginning in November. We expect as time passes, the lower dollar will cause the **trade deficit** to narrow but politicians are not willing to wait and let markets work. They want to intervene by **reducing imports** by imposing fees on those imports and causing import prices to rise. This kind of **intervention** would lead to higher inflation due to rising import prices and create room for domestic producers to raise prices to offset **rising labor costs**. Patience is not a quality of politicians. **Inflation risk** increases with this kind of reaction.

The data due out this week will be dominated by the **labor market report** on Friday. **Job growth** is expected to be robust for February with **nonfarm payrolls** increasing about the same as the January report. The key issue will be **average hourly earnings**. The rising inflation risks started with a rise in average hourly earnings reported for December as investors believed this was the beginning of much stronger growth in labor costs from a very tight labor market. We are close to **full employment** and that condition always leads to **higher inflation rates**. The consensus forecast calls for a moderate increase in hourly earnings at only 0.2% for the month. This would result in no change to the Y/Y increase of 2.9% from last month's report. Should the growth come in at 0.3% or higher, **inflation risk** would rise even more than what is currently being priced into **market interest rates**. This would drive the **Fed** to move managed rates up more and faster than their current guidance. The issue we continue to face is the disconnection between fundamentals which have driven **economic growth** in the past. This disconnect was highlighted last week with a strong **consumer confidence** report and a modest increase in **personal spending**. A tight labor market with job prospects continuing to improve and high levels of confidence has historically led to a surge in **consumer spending**. The **ISM Index** has been a very reliable indicator of future manufacturing activity and rising **durable goods orders**. The **ISM Index** was at a 14 year high while industrial production and durable goods orders were weak. Again, patience is required for the fundamentals to drive both economic growth and inflation.