THE AUSTIN ADVISOR

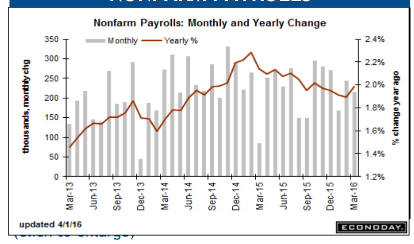
May 2, 2016

Markets	25-Apr	26-Apr	27-Apr	28-Apr	29-Apr	YTD%	31-Dec-15
DJIA	17,977.24	17,990.32	18,041.55	17,830.76	17,773.64	2.00%	17,425.03
S&P 500	2,087.79	2,091.70	2,095.15	2,075.81	2,065.30	1.04%	2,043.94
NASDAQ	4,895.79	4,888.28	4,863.14	4,805.29	4,775.36	-4.63%	5,007.41
SNL Bank Index	410.06	414.07	414.28	409.65	406.53	-5.78%	431.48
Fed Funds Rate	0.37%	0.37%	0.37%	0.37%	0.30%		0.35%
1 Month LIBOR	0.44%	0.44%	0.44%	0.44%	0.44%		0.43%
3 Month LIBOR	0.63%	0.63%	0.64%	0.64%	0.64%		0.61%
3 Month T-Bill	0.25%	0.24%	0.24%	0.22%	0.22%		0.16%
1 Year Treasury	0.57%	0.61%	0.58%	0.56%	0.56%		0.65%
2 Year Treasury	0.85%	0.86%	0.83%	0.78%	0.77%		1.06%
3 Year Treasury	1.01%	1.04%	0.99%	0.93%	0.92%		1.31%
5 Year Treasury	1.38%	1.40%	1.33%	1.28%	1.28%		1.76%
10 Year Treasury	1.91%	1.94%	1.87%	1.84%	1.83%		2.27%
30 Year Treasury	2.72%	2.76%	2.71%	2.68%	2.66%		3.01%

WEEKLY HIGHLIGHT

The differences between financial markets and reported economic data continues to get wider

NONFARM PAYROLLS



Economy	Week of April 25, 2016	
New Home Sales	511,000	Slightly below consensus forecasts, but still a reasonable number relative to the past year's data
Durable Goods Orders	0.8%	Another reasonable number, but not reflective a solid rebound from the 3.1% decline reported for February
Consumer Confidence	94.2	Down from 96.1, led by a strong labor market sector, with confidence better than the actual spending growth
FOMC Meeting Ends		No change in monetary policy,with no indication the Fed is going to raise rates in June
Real GDP-Advance Report	0.5%	The Advance report was as weak as expected, but we expect upward revisions in the next two months
Personal Income	0.4%	Income growth is beginning to accelerate, as a tight labor market drives wage rates higher
Personal Spending	0.1%	Spending on a non-inflation adjusted basis remains low, with low prices masking the unit volume increases
PCE Core Price Index	0.1%	A lower number than we expected, bringing the YOY increase down to 1.6%

MONDAY MUSING

The picture below was captured during a recent ALCO teleconfernce with our Chief Economist, Bob Morgan.

Thanks to Greg, our longtime client, for capturing this classic moment.

Calendar	Release	Covering	Week of May 2, 2016
ISM Index	Monday	April	The index moved above the breakeven of 50 two months ago, and is expected to remain above it for April
Motor Vehicle Sales	Tuesday	April	Total sales are expected to remain above 17 million on an annual basis, which is a strong level of demand
Trade Deficit	Wednesday	March	A decline in the monthly deficit is expected at just $41.4 billion, as the inflation adjusted deficit continues to expand
Unemployment Rate	Friday	April	A drop back to 4.9% from 5.0% is expected, as the surge in the size of the labor force abates
Nonfarm Payrolls	Friday	April	Another month of job growth at the monthly average of 215,000 of the last year is expected
Avg. Hourly Earnings	Friday	April	An increase of 0.3% would continue the rising level of wages that began in late 2015
Consumer Credit	Friday	March	The growth in consumer borrowing has been largely limited to student and auto loans, expect +$15.3 billion

Commentary

The mixed economic and financial market conditions continue to be released. We have **the Fed** unwilling to take the next step in **normalizing monetary policy,** while the US economy is reported as having increased by 0.5% in the first quarter of the year. That rate of growth is the same as growth reported by the EU for Europe in the first quarter. The Worldwide economy continues to struggle to gain any momentum according to the data. At the same time, **job growth** remains strong, **inflation** pressures are building and incomes are beginning to grow at a faster pace. These conditions are at odds with each other. It is difficult to understand how rising employment levels and better income growth, combined with a reasonable level of **consumer confidence** does not generate faster overall economic growth. **Real GDP growth** was hindered by a steep drop in business fixed investment, and only a modest (less than 2%) growth in **personal consumption expenditures** in the first quarter.

We do expect Real GDP growth to be revised upward in the next two months, as more complete data on **personal spending** and the **trade deficit** are released. The dollar has dropped in the last month and that should limit the expansion of the trade deficit going forward. Personal spending should grow at a faster pace (above 3%) in the last three quarters of the year, with strong job prospects and rising wages contributing to faster growth in **final demand**. The jobs report for April due out this Friday should provide further evidence of these fundamental improvements. The increasing inflation pressures should be reported in the coming months as rising commodities (led by oil) begin to drive prices higher in the **CPI** and **PPI**. Oil is now trading around $45 barrel, up from under $30 only two months ago. This increase in the price has developed even as **OPEC** failed to reach an agreement on production limits. Rising commodity prices and rising job levels are not reflective of an economy growing at less than 1%. Investors are not demanding any inflation premium in current market interest rates to cover rising inflation in the next year. The Fed is not worried about inflation as of yet. The question is which will begin to price higher inflation in first.

At this point it appears the market will move before the Fed. That would mean a steepening **yield curve** in the short run, as market rates move up before the Fed moves short rates. Rising **funding costs** have begun for banks in many markets, as larger banks begin to try to change the mix of their funding portfolio to comply with new liquidity measures dictated by regulators. They are trying to grow **core retail deposits** to a larger percentage of total funding. This process is going to be difficult since these larger banks have been losing core retail deposits, as they have closed branches and increased fees on deposit products in the last few years. The large banks must reverse a trend and they will only be able to do that by buying market share. The large banks will be aggressive in pricing up deposit offering rates to gain the growth they need to meet the new funding limits coming into effect in 2018 and 2019. We have already experienced rising deposit offering rates in many markets led by the big banks. Now we need to get market interest rates higher in order to get some discipline in loan pricing.

Trusted Advisor to Financial Institutions
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