

THE AUSTIN ADVISOR

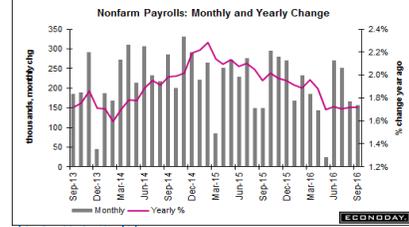
October 31, 2016

Markets	24-Oct	25-Oct	26-Oct	27-Oct	28-Oct	YTD%	31-Dec-15
DJIA	18,223.03	18,169.27	18,199.33	18,169.68	18,161.19	4.22%	17,425.03
S&P 500	2,151.33	2,143.16	2,139.43	2,133.04	2,126.41	4.03%	2,043.94
NASDAQ	5,309.83	5,283.40	5,250.27	5,215.97	5,190.10	3.65%	5,007.41
SNL Bank Index	429.36	429.10	431.69	433.27	430.66	-0.19%	431.48
Fed Funds Rate	0.41%	0.41%	0.41%	0.41%	0.41%		0.35%
1 Month LIBOR	0.53%	0.54%	0.53%	0.53%	0.53%		0.43%
3 Month LIBOR	0.88%	0.89%	0.89%	0.89%	0.89%		0.61%
3 Month T-Bill	0.33%	0.34%	0.33%	0.30%	0.30%		0.16%
1 Year Treasury	0.66%	0.66%	0.67%	0.68%	0.66%		0.65%
2 Year Treasury	0.84%	0.86%	0.86%	0.87%	0.86%		1.06%
3 Year Treasury	1.00%	1.00%	1.01%	1.04%	1.02%		1.31%
5 Year Treasury	1.27%	1.29%	1.30%	1.33%	1.33%		1.76%
10 Year Treasury	1.77%	1.77%	1.79%	1.85%	1.86%		2.27%
30 Year Treasury	2.52%	2.50%	2.53%	2.60%	2.62%		3.01%

WEEKLY HIGHLIGHT

The FOMC meets this week with stronger economic data and the expectation they move rates in Dec.

NONFARM PAYROLLS



Economy

Week of October 24, 2016

Consumer Confidence	98.6	The retreat from post recession highs was more than expected with the political environment, offset by solid job growth
New Home Sales	593,000	Sales were up from a revised August number, but well below the peak of this summer
Durable Goods Orders	-0.1%	No growth in the capital spending sector continues to be reflected with data like this
Real GDP-Advance Report	2.9%	The first look at the third quarter was better than expected on a narrowing trade deficit and better business fixed investment

MONDAY MUSING

I was doing volunteer work on a Habitat for Humanity project last week. Two young people were nailing siding on the house. One on them was reaching into the box of nails and throwing every other nail down on the ground. I asked why and was told "some of the nails were defective since they had the head on the wrong end". The other person said, "you idiot, those are for the other side of the house". (please note: this is a gender neutral story)

Calendar

Week of October 31, 2016

	Release	Covering	
Personal Income	Monday	September	The data was released before this update is written and came in at +0.3%, which is up from 0.2% in August
Personal Spending	Monday	September	Spending was reported at +0.5%, which is a strong rebound from the revised -0.1% in August
PCE Core Price Index	Monday	September	The monthly increase was 0.1% and does not change the 1.7% YOY change or below the Fed's target of 2%
Motor Vehicle Sales	Tuesday	October	Sales have leveled at 17.3 million, and we expect another month of that number
ISM Index	Tuesday	October	The index popped up above 50 two months ago and is expected to be little changed from the 51.5 reported for September
FOMC Announcement	Wednesday		No change in monetary policy is expected from this meeting, but signals about future moves will move markets
Unemployment Rate	Friday	October	After moving back to 5% in September on growth of workforce, the rate is forecast to drop back to 4.9%
Nonfarm Payrolls	Friday	October	The consensus calls for growth of 180,000, which is better than the last two months
Avg Hourly Earnings	Friday	October	Expectatons are for an increase of 0.3%, which is above the trend line of the past two years
Trade Deficit	Friday	September	A narrowing of the deficit is expected from -\$40.7B to -\$38.7B, as exports jumped at the end of the summer

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Commentary

Our forecast called for third quarter **Real GDP** growth to be 3.1%. The advance report last week came in at 2.9%. The advance report is always subject to large revisions as more complete data becomes available. The revisions over the past two years have been upward, and we expect that will be the case this time. The estimate for **personal consumption expenditures** for the quarter was only 2.1%. This is less than half the rate of growth for the second quarter of 4.3%. The third quarter report was an estimate since the final September data had not been released. We expect another upward revision to the GDP data as the PCE estimate is revised higher. The 2.9% growth estimate was driven up by a large expansion of exports bringing the drag from the trade deficit down, growth of inventories as opposed to a decline in the second quarter and an increase in business fixed investment (primarily in structures), as opposed to the drag of drops in the second quarter. Seventy percent of Real GDP is **consumer final demand** and we know September was much stronger than August. This rebound in September was probably understated in the advance report. The data was stronger than anticipated and will affect the Fed's action.

The **FOMC** meets this week with no one expecting the Fed to change monetary policy. This is not a meeting with a press conference following and the Fed would be unlikely to change policy this close to the election. The **consumer confidence index** computed by the Conference Board has consistently been higher than other survey's, but it did drop in October from the highest reading since the recession. Much of this decline was driven by the political environment, since the component dealing with the outlook for job growth remains very positive. This drop in the index will not have an impact on the Fed's decision this week. The key will be any signal sent with the language in the Fed's announcement at 2 pm on Wednesday.

In the face of this data, market interest rates have begun to move. Intermediate and long-term interest rates have moved up by 25 basis points in the last month, while short rates have remained the same. The **yield curve** has steepened. We have long maintained that banks cannot generate an increase in earnings in 2017 unless the curve steepens. This move in the curve reflects investors beginning to price an increase in inflation going forward more than the expectation of the Fed moves beginning in December. The small increase in the core PCE price index did not confirm this increase in inflation has begun as of yet. The question this week is whether the news in the election process will cause uncertainty for equity prices and impact the bond market. There is no way to forecast this possibility.

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