THE AUSTIN ADVISOR

December 14, 2015

Markets	7-Dec	8-Dec	9-Dec	10-Dec	11-Dec	YTD%	31-Dec-14
DJIA	17,730.51	17,568.00	17,492.30	17,574.75	17,265.21	-3.13%	17,823.07
S&P 500	2,077.07	2,063.59	2,047.62	2,052.23	2,012.37	-2.26%	2,058.90
NASDAQ	5,101.81	5,098.24	5,022.87	5,045.17	4,933.47	4.17%	4,736.05
SNL Bank Index	446.29	438.58	433.83	435.31	424.74	-1.85%	432.75
Fed Funds Rate	0.13%	0.13%	0.14%	0.14%	0.14%		0.06%
1 Month LIBOR	0.29%	0.29%	0.30%	0.32%	0.33%		0.17%
3 Month LIBOR	0.48%	0.49%	0.49%	0.50%	0.51%		0.26%
3 Month T-Bill	0.29%	0.27%	0.26%	0.24%	0.23%		0.04%
1 Year Treasury	0.67%	0.76%	0.72%	0.71%	0.68%		0.25%
2 Year Treasury	0.94%	0.94%	0.93%	0.95%	0.88%		0.67%
3 Year Treasury	1.24%	1.25%	1.22%	1.25%	1.16%		1.10%
5 Year Treasury	1.67%	1.68%	1.64%	1.68%	1.56%		1.65%
10 Year Treasury	2.23%	2.24%	2.22%	2.24%	2.13%		2.17%
30 Year Treasury	2.95%	2.97%	2.97%	2.98%	2.87%		2.75%

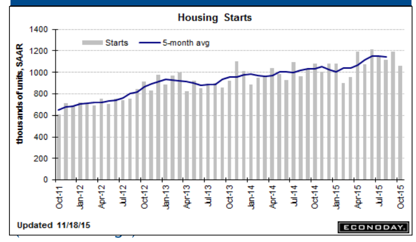
Economy		Week of December 7, 2015
Consumer Credit	$16.0 Billion	Less than expected, as credit card balances barely increased, but auto and student loans continue to grow
Producer Price Index	0.3%	Service sector price increases more than offset the decline in the commodity sector to produce a rise overall
Retail Sales	0.2%	The headline number was not very good, but the internal data in the report were very good

Calendar	Release	Covering	Week of December 14, 2015
Consumer Price Index	Tuesday	November	The core rate has shown some upward pressure in the last two months, and is expected to be up another 0.2%
Housing Starts	Wednesday	November	Starts are forecast to rebound in November after the decline in October, with the consensus at 1.141M, up from 1.060M
Industrial Production	Wednesday	November	Manufacturing has slowed due to the strong dollar and its impact on exports, with a drop of 0.2% expected
Capacity Utilization	Wednesday	November	Inflation pressures are not building, with an operating rate of 77.5%, as manufacturing continues weak
FOMC Meeting	Wednesday		A 2 pm announcement, followed by the Chairwoman's press conference, is scheduled
Leading Indicators	Thursday	November	The index has dropped in the past year, but did jump 0.6% in October and is forecast to be up 0.2% for November

WEEKLY HIGHLIGHT

The FOMC meeting this week is expected to result in the first increase in managed rates in over seven years

HOUSING STARTS



MONDAY MUSING

I am getting tired of Donald Trump. He is limiting the stories I can tell each week since some of them are politically incorrect. For example, How many Irishmen does it take to screw in a light bulb? None, they are perfectly happy to drink in the dark. What made me think of this was an experience from last week. I was sitting at a bar waiting for a friend, when a fly landed in the beer of the guy sitting next to me. The guy reached in the beer, grabbed the fly, and began squeezing it and yelling, "Spit it out, all of it". Turns out the guy was Irish. I cannot tell these stories as long as Trump keeps slamming everyone who does not look like him.

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Commentary

The FOMC meets this week with conflicting data on which they must make a decision about the direction of **monetary policy**. The volatility in the stock market last week, and continued weak economic data coming from China and Europe, takes us back to the September meeting. At that time investors expected **the Fed** to move up 25 basis points, but they cited financial market volatility and global economic uncertainty as reasons to leave monetary policy unchanged. Adding to the uncertainty for this meeting is the huge drop in **oil prices,** as inventories continue to expand. This raises the possibility of **deflation** in some forecasters view, and reduces the chances the Fed begins to normalize monetary policy. For all of the concern about issues like the strong dollar, the slowing **manufacturing sector** and the volatility in stock prices, we do expect the Fed to move on Wednesday.

The **U.S. economy** is doing better with each quarter of data. It is being led by the growth in **consumer final demand**. **The retail sales** data released last Friday is a reflection of this strength. The headline growth number was only 0.2% for November, but that is misleading. The sales data is not inflation adjusted, so the drop in gasoline prices causes the sales data to be lower even if the unit purchases grow. Additionally, the volatile **auto sales** data on a monthly basis affects the overall data. Retail sales were up 0.4% in November, excluding autos, and up 0.5% excluding both autos and gasoline. That is a solid growth number and reflects growing levels of **consumer spending**. Solid job growth and higher growth in wages, as the labor market tightens, should fuel continued growth in final demand and provide the basis for better **Real GDP** growth in 2016 than in 2015, even as the Fed raises short term interest rates. **Market interest rates** dropped last week, as capital flowed from stocks and into the safety of short term bonds. Capital also came from the high risk junk bond sector when a fund closed redemptions due to lack of liquidity in that market.

The economy is in a position to withstand the anticipated Fed action on short-term rates without slipping into recession. The argument is without some sign of **inflation**, there is no reason to run any risk to the economy by raising rates. We believe the tighter labor market will lead to rising wages. Higher **labor costs** will lead to some inflation increases going forward. We are not expecting inflation to reach unacceptable levels, but we forecast it goes above the Fed's target of 2% in 2016. We expect a 25 basis point increase on Wednesday. Market reaction will depend on the tone of the press conference which follows this meeting. We expect that **Chairwoman Yellen** will concentrate on the slow and gradual nature of the Fed's future action, in an effort to dampen any market reaction to this first step in moving borrowing costs to levels that better reflect the underlying economic fundamentals.

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