THE AUSTIN ADVISOR

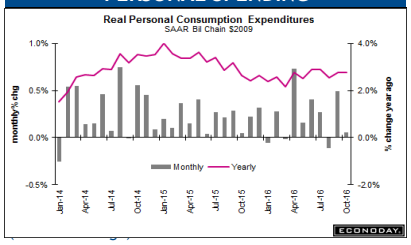
December 20, 2016

Markets	12-Dec	13-Dec	14-Dec	15-Dec	16-Dec	YTD%	31-Dec-15
DJIA	19,796.43	19,911.21	19,792.53	19,852.24	19,843.41	13.88%	17,425.03
S&P 500	2,256.96	2,271.72	2,253.28	2,262.03	2,258.07	10.48%	2,043.94
NASDAQ	5,412.54	5,463.83	5,436.67	5,456.86	5,437.16	8.58%	5,007.41
SNL Bank Index	531.58	532.51	529.59	536.65	531.32	23.14%	431.48
Fed Funds Rate	0.41%	0.41%	0.41%	0.66%	0.66%		0.35%
1 Month LIBOR	0.69%	0.70%	0.71%	0.74%	0.74%		0.43%
3 Month LIBOR	0.96%	0.96%	0.97%	0.99%	1.00%		0.61%
3 Month T-Bill	0.51%	0.54%	0.55%	0.51%	0.51%		0.16%
1 Year Treasury	0.85%	0.88%	0.92%	0.91%	0.91%		0.65%
2 Year Treasury	1.15%	1.17%	1.27%	1.29%	1.28%		1.06%
3 Year Treasury	1.44%	1.46%	1.57%	1.61%	1.59%		1.31%
5 Year Treasury	1.90%	1.92%	2.02%	2.10%	2.07%		1.76%
10 Year Treasury	2.49%	2.48%	2.54%	2.60%	2.60%		2.27%
30 Year Treasury	3.16%	3.14%	3.14%	3.16%	3.19%		3.01%

WEEKLY HIGHLIGHT

The Fed did move managed rates up and did not include possible fiscal stimulus in their forecasts

PERSONAL SPENDING



Economy	Week of December 12, 2016	
Producer Price Index	0.4%	The increase was twice the expected result, despite a decline in energy prices, which fed inflation risks
Retail Sales	0.1%	A much weaker number than expected, caused by a decline in auto sales, with sales up 0.2% excluding autos
Industrial Production	-0.4%	The big drop was due to another big drop in utility output, but even excluding that output declined.
Capacity Utilization	75.0%	Down from 75.4%, as significant slack in manufacturing remains weak
FOMC Announcement		The Fed moved the target rate up 25 basis points as expected, and indicated more rate hikes are coming
Consumer Price Index	0.2%	The inflation risk increase being priced in the bond market has not yet been reflected in the data
Housing Starts	1.090 Million	Well below forecasts and down from 1.340M reported for October, as this highly volatile data remains sluggish

MONDAY MUSING

Christmas is a great time of the year. It is a time when each of us can worship by going to the mall of our choice. I once got a gift from my father that was a box of broken glass. My brother got a box of Band-Aids. The card told us to share. We must have had one too many fights. After wrapping all the presents, it appears Christmas has become a baby shower run amuck. I know I am in trouble since Santa now looks younger than I do. Have a Merry Christmas.

Calendar	Release	Covering	Week of December 19, 2016
Existing Home Sales	Wednesday	November	The lack of homes for sale is limiting activity, with a consensus of 5.535 million expected, down from 5.6M in October
Durable Goods Orders	Thursday	November	Following a large 4.8% jump in October forecasts are for a 4.1% drop, while excluding aircraft, are more stable
Real GDP - Final	Thursday	3rd Qtr	A small final revision to growth is expected with a 3.3% final number, up from 3.2% in the last report
Personal Income	Thursday	November	Incomes have been improving at a better rate, with 0.3% growth expected after a strong 0.6% reported for October
Personal Spending	Thursday	November	Spending is forecast to be solid, even with a small retail sales number, as service sector spending is strong
Core PCE Index	Thursday	November	Another small increase of 0.1% is expected, as inflation fears have not been realized yet
New Home Sales	Friday	November	With limited homes on the market, new home sales have been strong and another solid month of 580,000 is expected

THE AUSTIN ADVISOR

Commentary

In what may have been the most widely anticipated move ever, **the Fed** did raise the target rate for Fed Funds by 25 basis points last week. In the statement announcing the move, the Fed said they believed the economy had improved and we are approaching full employment. They also said **inflation** was near their target of 2%. They did not change their prior economic forecast, but did change their guidence for the number of anticipated increases in 2017 from two to three. They judged the economy was strong enough to absorb three increases without slowing growth. In the press conference that followed, **Chairwoman Yellen** said the committee did not consider any change in current **fiscal policy** in their decision. The proposed corporate tax cuts, increased spending programs, and reduced regulations were not an element of this move. The Fed said these possibilities were discussed, but the magnitude and timing of any of these fiscal stimulus programs were unknown and therefore not included in their forecasts or considerations. We do believe there will be significant fiscal stimulus early in 2017, which will boost economic growth and inflation. We know this is a political forecast and our opinion is no more valid than anyone else's. The bond market is already pricing in a rise in inflation in the next year. The steepening of the **curve**, with intermediate and long-term rates up more than short rates, is a reflection of the demand for a risk premium for inflation. The Fed is not there yet. As a result, the risk is the Fed moves more than three times next year and managed rates go above the levels we currently are forecasting. The timing and magnitude of the fiscal policy changes will dictate how much rates move up during the year.

We are having the usual problem with year-end and beginning seasonal adjustment factors. **Retail sales** were reported as having only increased by 0.1% for November. However, **auto sales** were reported as having been very strong for the month and service sector spending is not counted in retail sales. This spending will be reported this week as a part of **personal spending**. It is this data, which is seasonally adjusted, that will be used in the **GDP report** for the fourth quarter. The issue remains as to whether the move to on-line purchases are being fully captured in the spending data. The changes in the way consumers buy is causing issues with the quarterly data. Making decisions using one quarter's data can lead to mistakes on the overall strength of the total economy. We know this issue is being addressed, but we continue to look for volatile data in the fourth quarter of this year and the first quarter of next year.

Trusted Advisor to Financial Institutions
www.austinassociates.com
info@austinassociates.com