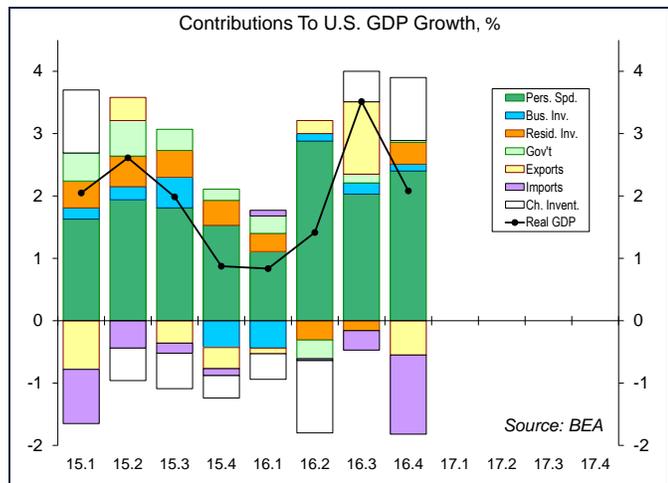


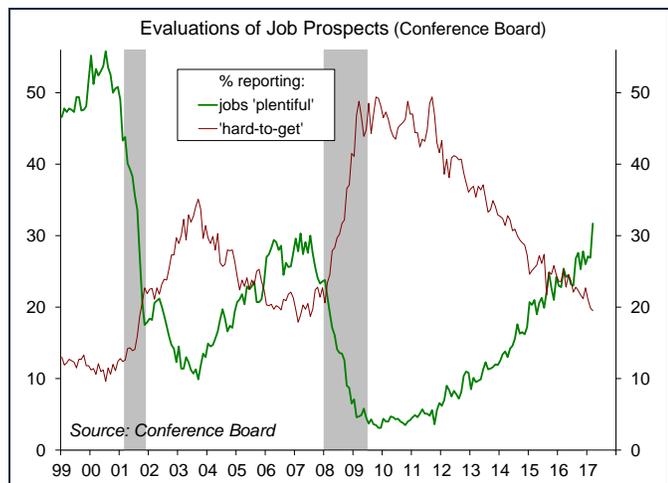
Weekly Economic Monitor

Consumer Stumble or Just a Pause?

Consumer spending accounts for 69% of Gross Domestic Product. Last week, the data on the household sector were mixed. The Conference Board's Consumer Confidence Index surged to a 16-year high. Meanwhile, inflation-adjusted consumer spending has been tracking at below a 1% annual rate in 1Q17. Does this spell trouble for the consumer? Or is this merely the pause that refreshes?



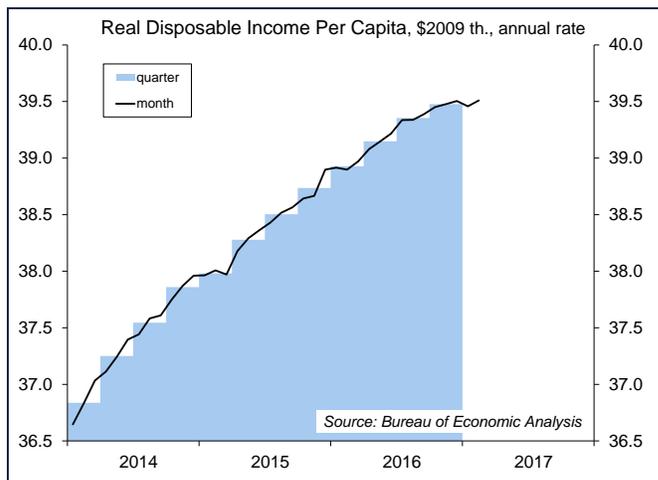
The 3<sup>rd</sup> estimate of 4Q16 GDP growth showed a stronger gain in consumer spending (a 3.5% annual rate). A year ago, spending was soft, but rebounded into 2Q16. Monthly figures through February suggest that inflation-adjusted spending is tracking at below a 1% annual rate. That's a sharp slowing, but doesn't look too terrible following a strong fourth quarter.



The Conference Board's Consumer Confidence Index surprised to the upside last week, rising to its highest level since December 2000. Other attitude measures have been mixed. Interestingly, the report on UM Consumer Sentiment continues

to show a sharp division on political persuasion. Democrats are depressed. Republicans are downright giddy (which remains a positive factor for the stock market). Getting a representative sample is a key issue for consumer surveys. A shift one way or the other in the composition can skew results.

Consumers don't spend confidence. Income is the key driver (wealth and the ability to borrow are also factors). While nominal (current dollar) average hourly earnings growth has been trending higher, real (inflation-adjusted) earnings are little changed relative to a year ago. Inflation-adjusted disposable income per capita has been trending about flat in recent months. That suggests limited firepower for consumer spending growth in the near term. This slowdown is likely to be temporary. Gasoline prices, up over the last year, have begun to stabilize in recent weeks (so y/y inflation is unlikely to be as high as it has been recently).



Other factors may have limited consumer spending growth recently. Delayed tax returns (relative to last year) have been widely reported. In addition, many households have health insurance plans with deductibles that reset once a year (often in January). This means more spending on prescriptions and doctor visits, and less money to spend on other things.

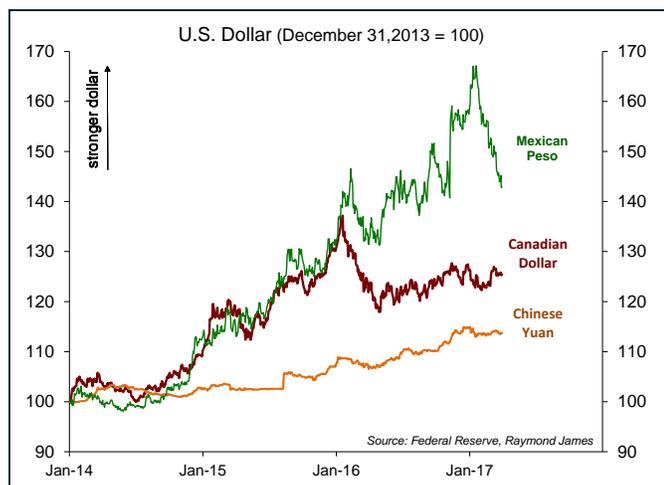
There were several tax aspects to the Affordable Care Act. Failure to repeal makes comprehensive tax reform unlikely, but we may see a reduction in tax rates in the months ahead. Still, tax cuts would be weighted toward the upper end of the income scale, and will provide little support for the typical worker.

As usual, the spring economic data will tell the tale. Keep a close eye on job and wage growth over the next couple of months. For the Fed, the focus is on the job market and the inflation outlook, but the outlook should remain consistent with a further normalization of monetary policy. Officials are likely to remain optimistic about growth despite the soft first quarter.

|         | Treasury Yields |       |       |      |      |      |       |       | Dollar  |       |        |       | Equities |         |          |
|---------|-----------------|-------|-------|------|------|------|-------|-------|---------|-------|--------|-------|----------|---------|----------|
|         | 13-wk           | 26-wk | 52-wk | 2-yr | 3-yr | 5-yr | 10-yr | 30-yr | \$/Euro | \$/BP | JY/\$  | CD/\$ | NASD     | SPX     | DJIA     |
| 3/03/17 | 0.71            | 0.84  | 0.98  | 1.32 | 1.59 | 2.02 | 2.49  | 3.08  | 1.055   | 1.225 | 114.60 | 1.342 | 5870.75  | 2383.12 | 21005.71 |
| 3/24/17 | 0.78            | 0.89  | 1.00  | 1.26 | 1.52 | 1.93 | 2.40  | 3.00  | 1.081   | 1.249 | 111.03 | 1.337 | 5828.74  | 2343.98 | 20596.72 |
| 3/31/17 | 0.76            | 0.90  | 1.03  | 1.26 | 1.50 | 1.93 | 2.40  | 3.02  | 1.067   | 1.252 | 111.34 | 1.330 | 5923.93  | 2362.70 | 20663.43 |

## Recent Economic Data and Outlook

Following the disappointment with Congress' ability to repeal the Affordable Care Act (which created doubts about the rest of the Trump agenda), stock market participants were looking for some good news and found it in the Consumer Confidence Index.



The White House appeared to soften its stance on **NAFTA**, suggesting improvement around the edges instead of a complete overhaul. At the same time, President Trump continued to talk tough on trade with China (note that Chinese President Xi will visit Mar-a-Lago on April 6 and 7).

U.K. Prime Minister Theresa May submitted the Article 50 letter to the European Union, starting a two-year period of **Brexit** negotiations. The pace of negotiations is expected to be most intense about a year from now, in order to allow the individual countries time to vote on the agreement.

**Real GDP** rose at a 2.1% annual rate in the 3<sup>rd</sup> estimate for 4Q16 (vs. +1.9% in both the advance and 2<sup>nd</sup> estimates). Real growth in consumer spending was revised to 3.5% (vs. 3.0% in the 2<sup>nd</sup> estimate and +2.5% in the advance estimate).

**Personal Income** rose 0.4% in February (+4.6% y/y), led by a 0.5% increase in private-sector wages and salaries (+6.0% y/y). Disposable income rose 0.3% (+4.4% y/y), up 0.2% adjusting for inflation (+2.3% y/y). **Personal Spending** edged up 0.1% (+4.8% y/y), down 0.1% adjusted for inflation (+2.6% y/y). The **PCE Price Index** rose 0.1% (+2.6% y/y), up 0.2% excluding food and energy (+1.8% y/y, inching closer toward the Fed's 2% goal).

**Jobless Claims** edged down to 258,000 in the week ending March 25, vs. 261,000 in the week before. The four-week average was 254,250, somewhat higher than the previous trend.

The Conference Board's **Consumer Confidence Index** jumped to 125.6 in the advance estimate for March (based on information collected on or before March 16). It was the highest level since December 2000. Evaluations of current job availability, which tend to lag actual labor market improvement by many months, rose to the best level since early 2001.

The University of Michigan's **Consumer Sentiment Index** full-month reading for March was 96.9, down from 97.6 at mid-month, but up from February's 96.3. The report highlighted the continued division on political affiliation, with democrats much more negative on evaluations of current conditions and on expectations for the future. The report noted that "it is a rare situation that combines increasing optimism, which promotes spending, as well as rising uncertainty, which makes consumers more cautious spenders."

The **Pending Home Sales Index** rose 5.5% in February, following a 2.8% drop in January. Results were improved across regions (+3.4% in the Northwest, +11.4% in the Midwest, +4.3% in the South, and 3.1% in the West).

The **Chicago Business Barometer** edged up to 57.7 in March, vs. 57.4 in February and 50.3 in January. The report noted a further strengthening in new orders and production, but employment slipped back into contraction.

**Economic Outlook (2Q17):** 2.0-2.5% GDP growth, following around 1.0% growth in 1Q17 (reflecting a much slower pace of consumer spending growth).

**Employment:** Job growth has remained relatively strong, although the pace should slow as the job market tightens.

**Consumers:** Job gains and wage growth are supportive, but purchasing power has decreased (gasoline prices). Debt levels are manageable, with few signs of strain in the aggregate.

**Manufacturing:** Improving in the near term, reflecting good weather, strengthening capital goods orders, and an improved global economic outlook.

**Housing/Construction:** Job growth has remained supportive, but higher home prices and higher mortgage rates are a restraint for first-time buyers. Tax cuts are expected to help fuel the demand for vacation homes and second homes.

**Prices:** Ex-food & energy, the PCE Price Index has continued to trend below the Fed's 2% target, but not by a lot. There is little inflation in consumer goods. Inflation in services has been boosted by higher rents. Wage gains are moderate, but rising.

**Interest Rates:** The Fed remains in tightening mode, and is expected to be more aggressive in raising rates in 2017 than in 2016 and 2015, but policy will remain data-dependent.

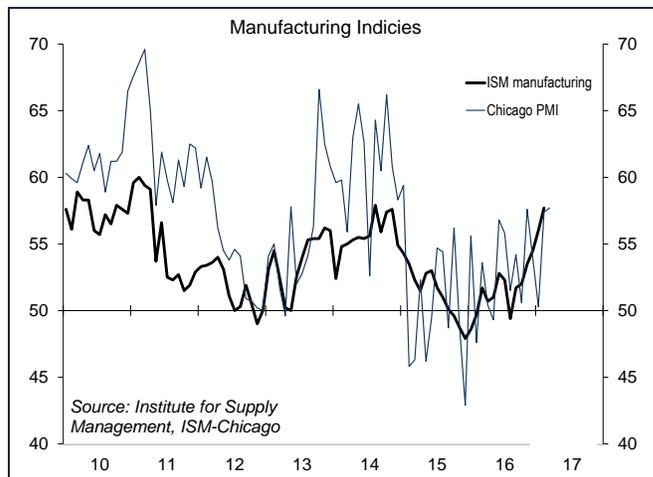
| This Week:        |      |       |   | <i>forecast</i> | last         | last -1    | comments |   |
|-------------------|------|-------|---|-----------------|--------------|------------|----------|---|
| Monday            | 4/03 | 10:00 | Construction Spending                       | Feb             | <b>NF</b>    | -1.0%      | +0.1%    | should be higher                          |
|                   |      | 10:00 | <b>ISM Manf. Index</b>                      | Mar             | <b>56.4</b>  | 57.7       | 56.0     | moderately strong                         |
|                   |      | tba   | Motor Vehicle Sales, mln domestically built | Mar             | <b>17.3</b>  | 17.5       | 17.5     | weather may have been a factor            |
|                   |      |       |   |                 | <b>13.4</b>  | 13.6       | 13.6     | trend is flattening                       |
| Tuesday           | 4/04 | 8:30  | Trade Balance, \$bln goods only             | Feb             | <b>-44.7</b> | -48.5      | -44.3    | narrower in Feb (vs. wider in Jan)        |
|                   |      | 10:00 | Factory Orders                              | Feb             | <b>+0.9%</b> | +1.4%      | +1.3%    | imports have been rising                  |
|                   |      |       |   |                 |              |            |          | durable goods orders reported up +1.7%    |
| Wednesday         | 4/05 | 8:15  | <b>ADP Payroll Estimate, th.</b>            | Mar             | <b>+170</b>  | +298       | +261     | were Mar gains pulled into Feb?           |
|                   |      | 10:00 | <b>ISM Non-Manf. Index</b>                  | Mar             | <b>56.5</b>  | 57.6       | 56.5     | moderately strong                         |
|                   |      | 2:00  | <b>FOMC Minutes</b>                         | 3/15            |              |            |          | looking for clues on possible June hike   |
| Thursday          | 4/06 | 8:30  | Jobless Claims, th.                         | 4/01            | <b>245</b>   | 258        | 261      | a bit higher in last two weeks            |
| Friday            | 4/07 | 8:30  | <b>Nonfarm Payrolls, th.</b>                | Mar             | <b>+170</b>  | +235       | +238     | seen somewhat slower (weather?)           |
|                   |      |       | private-sector                              |                 | <b>+170</b>  | +227       | +221     | still relatively strong                   |
|                   |      |       | <b>Unemployment Rate</b>                    |                 | <b>4.7%</b>  | 4.7%       | 4.8%     | seen steady or slightly lower             |
|                   |      |       | employment/population                       |                 | <b>60.0%</b> | 60.0%      | 59.9%    | trending gradually higher                 |
|                   |      |       | Avg. Weekly Hours                           |                 | <b>34.3</b>  | 34.4       | 34.4     | there may be some weather impact          |
|                   |      |       | Avg. Hourly Earnings                        |                 | <b>+0.3%</b> | +0.2%      | +0.2%    | moderate wage pressures                   |
| <b>Next Week:</b> |      |       |   |                 |              |            |          |   |
| Monday            | 4/10 | 1:00  | Treasury Note Auction                       |                 |              |            |          | 3-year notes                              |
| Tuesday           | 4/11 | 6:00  | Small Business Optimism                     | Mar             | <b>NF</b>    | 105.3      | 105.9    | still strong                              |
|                   |      | 10:00 | JOLTS: hiring rate                          | Feb             | <b>NF</b>    | 4.1%       | 4.1%     | trending about flat, but moderately high  |
|                   |      | 10:00 | JOLTS: quit rate                            | Feb             | <b>NF</b>    | 2.5%       | 2.4%     | highest since before the recession        |
|                   |      | 1:00  | Treasury Note Auction                       |                 |              |            |          | re-opened 10-year notes                   |
| Wednesday         | 4/12 | 8:30  | Import Prices                               | Mar             | <b>NF</b>    | +0.2%      | +0.6%    | petroleum prices lower                    |
|                   |      |       | ex-food & fuels                             |                 | <b>NF</b>    | +0.3%      | 0.0%     | mild trend otherwise                      |
|                   |      | 10:00 | BOC Policy Decision                         |                 |              |            |          | steady, but pressure to follow the Fed    |
|                   |      | 1:00  | Treasury Bond Auction                       |                 |              |            |          | re-opened 30-year bonds                   |
| Thursday          | 4/13 | 8:30  | Jobless Claims, th.                         | 4/08            | <b>245</b>   | <b>245</b> | 258      | still a low trend                         |
|                   |      | 8:30  | <b>Producer Price Index</b>                 | Mar             | <b>+0.1%</b> | +0.3%      | +0.6%    | seas adj amplifies gasoline price decline |
|                   |      |       | <b>ex-food &amp; energy</b>                 |                 | <b>+0.2%</b> | +0.3%      | +0.4%    | moderate old core                         |
|                   |      |       | <b>ex-f, e, trade services</b>              |                 | <b>+0.2%</b> | +0.3%      | +0.2%    | moderate new core                         |
|                   |      | 10:00 | UM Consumer Sentiment                       | m-Apr           | <b>95.6</b>  | 96.9       | 96.3     | seen somewhat lower                       |
|                   |      | 2:00  | SIFMA: early bond close                     |                 |              |            |          | full session for the stock market         |
| Friday            | 4/14 |       | Good Friday Holiday                         |                 |              |            |          | markets closed                            |
|                   |      | 8:30  | <b>Consumer Price Index</b>                 | Mar             | <b>+0.0%</b> | +0.1%      | +0.6%    | seas adj amplifies gasoline price decline |
|                   |      |       | year-over-year                              |                 | <b>+2.6%</b> | +2.7%      | +2.5%    | reflects higher energy costs              |
|                   |      |       | <b>ex-food &amp; energy</b>                 |                 | <b>+0.2%</b> | +0.2%      | +0.3%    | moderate core inflation                   |
|                   |      |       | year-over-year                              |                 | <b>+2.3%</b> | +2.2%      | +2.3%    | trending higher than core PCE Price Index |
|                   |      | 8:30  | Real Hourly Earnings                        | Mar             | <b>NF</b>    | +0.1%      | -0.4%    | should pick up                            |
|                   |      | 8:30  | <b>Retail Sales</b>                         | Mar             | <b>+0.4%</b> | +0.1%      | +0.6%    | moderate                                  |
|                   |      |       | <b>ex-autos</b>                             |                 | <b>+0.3%</b> | +0.2%      | +1.2%    | lower gasoline prices                     |
|                   |      |       | <b>ex-autos, bld mat, gasoline</b>          |                 | <b>+0.4%</b> | 0.0%       | +0.9%    | moderate                                  |
|                   |      | 10:00 | Business Inventories                        | Feb             | <b>+0.3%</b> | -0.1%      | +0.4%    | pace seen slower in 1Q17                  |

## This Week...

March economic data begin to arrive. While there may be some reaction to the ISM survey results (if far enough from expectations), the focus ought to be on the employment report. Mild weather likely pulled some seasonal job gains forward into February, and snowstorms, during the payroll survey period, may dampen both jobs and hours in March (if so, the BLS should make a note of that in the report). FOMC minutes should show a majority of policymakers on board for further rate increases – and June rate hike odds may move up.

## Monday

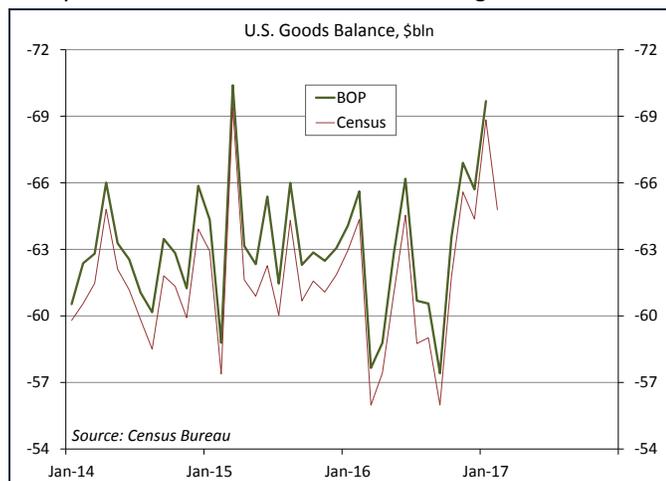
**ISM Manufacturing Index (March)** – Expected to remain relatively strong in March. Watch new orders and employment.



**Motor Vehicle Sales (March)** – Auto production and sales, which had fallen sharply during the financial crisis, were a key factor in the economic recovery. However, while there will surely be some variation in the pace of sales from month to month, the underlying trend appears to have plateaued.

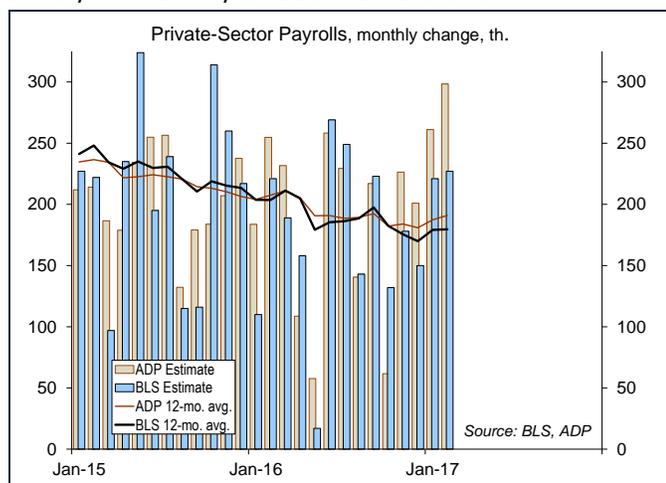
## Tuesday

**Trade Balance (February)** – The advance merchandise trade figures showed that the trade deficit narrowed in February, after widening sharply in January. Hence, net exports appear unlikely to subtract as much from 1Q17 GDP growth.



## Wednesday

**ADP Payroll Estimate (March)** – The ADP estimate of private-sector payrolls rose faster than the BLS estimate in January and February. We're likely to see some moderation.



**ISM Non-Manufacturing Index (March)** – The headline figure is expected to remain relatively strong. Details should be consistent with moderate economic growth in the near term.

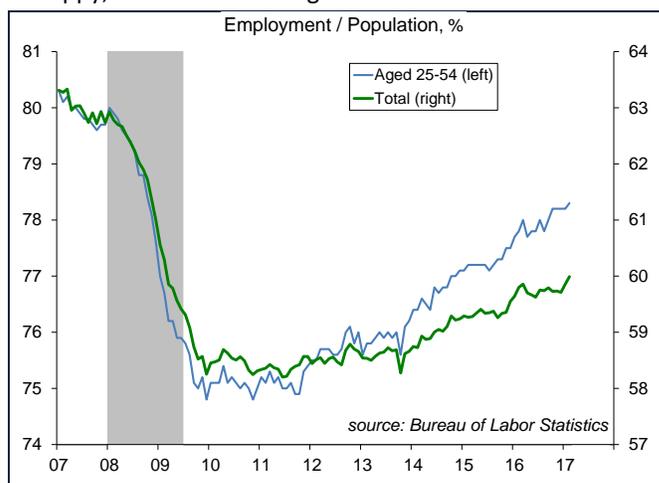
**FOMC Minutes (March 14-15)** – We aren't likely to learn much that is new in the minutes of the mid-March policy meeting. The majority of senior Fed officials (not all of whom vote on monetary policy) are in the more-aggressive tightening camp. That doesn't mean that the Fed is slamming on the brakes. Future rate hikes are likely to come gradually (meaning that it's up to the data to dissuade the Fed from a June hike).

## Thursday

**Jobless Claims (week ending April 1)** – Claims picked up a bit in the two previous weeks, possibly reflecting an impact of earlier snowstorms (which initially delay filings, but then rises following the weather's negative impact on growth).

## Friday

**Employment Report (March)** – The weather was generally mild in February, which likely contributed to the strong gain in nonfarm payrolls. Some strength may have been borrowed from March and April. Snowstorms arrived during the payroll survey week, which may depress the total somewhat (the Bureau of Labor Statistics is usually good at picking up on any weather effects). The unemployment rate should hold roughly steady (although is reported accurate to  $\pm 0.2\%$ ). Average hourly earnings tend to be choppy, but the trend is higher.



## Next Week ...

The important data (CPI, retail sales) will show up on Friday, but the financial markets will be closed.

## Coming Events and Data Releases

|              |   |
|--------------|---|
| April 18     | Building Permits, Housing Starts (March)      |
| April 19     | Fed Beige Book                                |
| April 28     | Real GDP (1Q17, advance)                      |
| May 3        | FOMC Policy Decision (no press conference)    |
| May 5        | Employment Report (April)                     |
| June 14      | FOMC Policy Decision, Yellen press conference |
| July 26      | FOMC Policy Decision (no press conference)    |
| September 20 | FOMC Policy Decision, Yellen press conference |
| November 1   | FOMC Policy Decision (no press conference)    |
| December 13  | FOMC Policy Decision, Yellen press conference |