THE AUSTIN ADVISOR

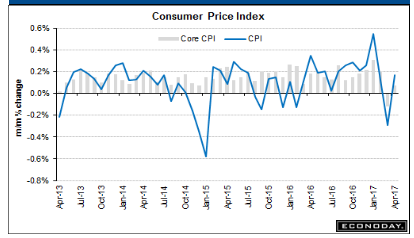
June 12, 2017

Markets	5-Jun	6-Jun	7-Jun	8-Jun	9-Jun	YTD%	30-Dec-16
DJIA	21,184.04	21,136.23	21,173.69	21,182.53	21,271.97	7.64%	19,762.60
S&P 500	2,436.10	2,429.33	2,433.14	2,433.79	2,431.77	8.62%	2,238.83
NASDAQ	6,295.68	6,275.06	6,297.38	6,321.76	6,207.92	15.32%	5,383.12
SNL Bank Index	515.72	513.82	519.40	528.54	541.82	1.72%	532.65
Fed Funds Rate	0.91%	0.91%	0.91%	0.91%	0.91%		0.55%
1 Month LIBOR	1.08%	1.09%	1.10%	1.12%	1.13%		0.77%
3 Month LIBOR	1.22%	1.22%	1.22%	1.23%	1.24%		1.00%
3 Month T-Bill	0.96%	0.97%	1.00%	1.01%	1.01%		0.51%
1 Year Treasury	1.16%	1.16%	1.17%	1.19%	1.20%		0.85%
2 Year Treasury	1.32%	1.30%	1.32%	1.33%	1.35%		1.20%
3 Year Treasury	1.45%	1.42%	1.45%	1.47%	1.50%		1.47%
5 Year Treasury	1.74%	1.71%	1.74%	1.75%	1.77%		1.93%
10 Year Treasury	2.18%	2.14%	2.18%	2.19%	2.21%		2.45%
30 Year Treasury	2.84%	2.81%	2.84%	2.85%	2.86%		3.06%

WEEKLY HIGHLIGHT

The FOMC meeting this week is expected to provide better guidence from the Fed

CONSUMER PRICE INDEX



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Economy	Week of June 5, 2017	
JOLTS	6.044 Million	Well above expectations and the gap between job openings and job growth is widening
Consumer Credit	$8.2 Billion	About half the expected increase, with auto loans and student loans well below the average monthly gain of the past two years

Calendar	Release	Covering	Week of June 12, 2017
Producer Price Index	Tuesday	May	Following the big 0.5% rise in April, only 0.1% is expected for May as inflation pressures remain muted
Consumer Price Index	Wednesday	May	In yet another indication inflation is well contained, no increase in the CPI is expected, keeping the core YOY at 1.9%
Retail Sales	Wednesday	May	After a solid gain of 0.4% in April, a modest increase of 0.2% is expected for May as consumer spending remains modest
FOMC Meeting Ends	Wednesday		The Fed ends its meeting with a strong consensus they will raise rates another 25 basis points
Industrial Production	Thursday	May	Another data point is expected to reflect a much softer growth environment in May from April, with only 0.2% expected
Capacity Utilization	Thursday	May	Little change in the 76.7% operating rate is expected, as it remains well below inflation levels
Housing Starts	Friday	May	The weaker starts data in April was in multi-family units with single family growth accelerating, expect 1.221 million

MONDAY MUSING

I was in Chicago last week and was riding an elevator in what used to be called the Sears tower. It caused me to remember a friend from years past who hated crowded elevators, so he came up with some ways to get people off. His favorite was to hold the doors open for 15 seconds and when nobody got on, he would let the doors close and say "George, what took you so long?". Sometimes he would stare at one of the other people and then scream, "you are one of those!!!". Finally, he would shake hands with everyone on the elevator and tell them to just call him Admiral. Each one of these would cause people to push buttons and get off as soon as possible. As I thought of these little fun things to do I started to laugh. I found laughing on an elevator also works.

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Commentary

The Fed meets this Tuesday and Wednesday. The announcement of any action will be made at 2:00 pm on Wednesday. The revised forecast of future economic expectations will be published at that time and the Fed Chairwoman's quarterly press conference will begin at 2:30 pm. The markets are expecting another increase in managed rates. Should this occur, it will be the third increase by the Fed in the past six months, taking the Funds rate up 75 basis points to over 1.0%. The bond market has priced in this move, with short-term rates up 20 basis points in the past month. The key to this move will be in the details of the language in the statement and the tone of the press conference. We expect the Fed to repeat the language of the last **FOMC** meeting by stating the weak **consumer spending** pattern of the past five months is transitory. The revised economic forecast should be lowered from past forecasts. The Fed will need evidence this weaker final demand environment is going to strengthen in the second half of the year. Therefore, we do not expect another move by the Fed until December. Final demand must be much stronger than the past five months in order to increase pricing pressures. Investors do not expect any **inflation** pressure since intermediate and long-term rates have declined in the past month.

The flattening **curve** is starting to put pressure on loan rates, with some banks quoting lower new loan rates than was the case just a month ago. The key question is whether this move by the Fed will cause an increase in competitive deposit rates. The first two increases by the Fed and the rise in short-term market rates has not resulted in an increase in posted deposit rates in the banking industry. Money market rates at banks are still below 25 basis points and savings accounts are generally below 10 basis points. These low offering rates are well below alternatives. For example, a 3 month treasury offers a yield above 1.0% and that is driving non-deposit alternatives like money market mutual funds to quote yields at or above 1.0%. This spread between bank deposit rates and alternatives is not causing depositors to move balances to take advantage of the higher yields available. In fact, for many of our community bank clients, balances have increased in these lower yielding accounts in the past six months. The risk is these competitive rates will begin to rise if depositors begin to shift balances to higher yielding alternatives and to special short-term CD offerings being made by some banks. Should this begin, bank net interest margins will come under pressure in the second half of the year. We have not seen a shift in deposit dollars as of yet and the question is whether this move by the Fed will cause it to begin.