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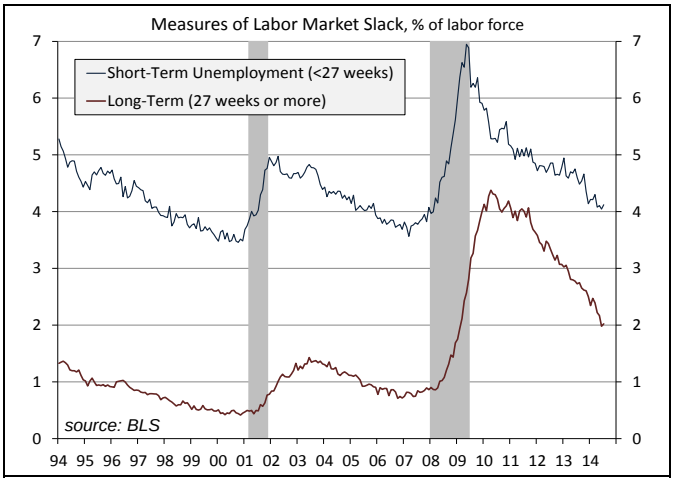
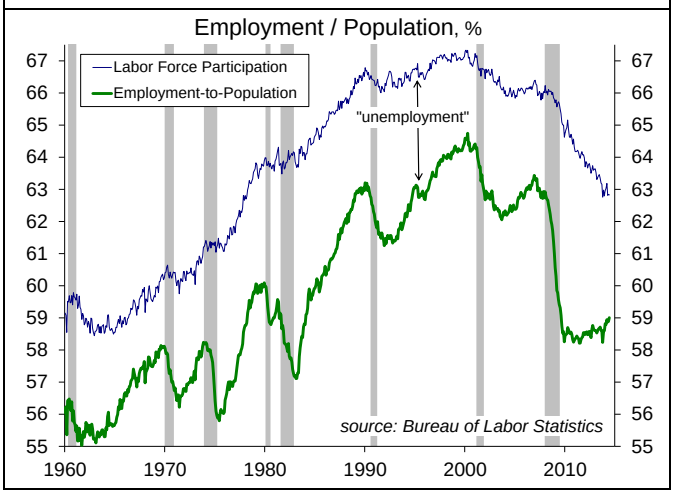
Weekly Market Monitor

How Much Slack Is There In the Job Market?

The amount of slack in the labor market will be a key driver of monetary policy in the months ahead. Fed officials differ in their perceptions of job market slack, leading some to want to tighten policy sooner rather than later. Labor market data can present somewhat different pictures, but on balance, there is still a large amount of slack remaining.

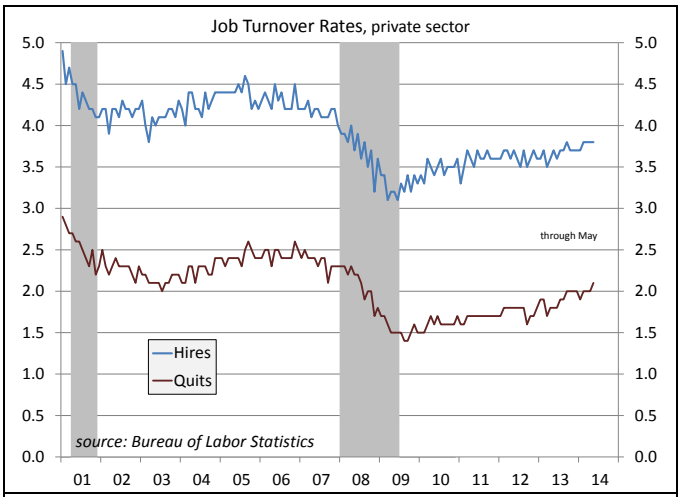
Weekly claims for unemployment insurance have been trending at very low levels, consistent with a limited pace of job destruction. Short-term unemployment is now at a "normal" level, consistent with the usual labor market frictions of a fully recovered job market. However, long-term unemployment and measures of underemployment remain elevated.





Labor force participation is the lowest since the 1970s. About a third of the decline since the recession began is due to demographics, the aging of the population. However, most of the decline is due to individuals who have given up looking for a job. However, as we learned in the strong job market of the late 1990s, the labor force is a lot more flexible than you might think. Rising wages could easily lure recent retirees and stay-at-home spouses back into the labor force.

Surveys of hiring intentions have shown gradual improvement in recent years, but remain below normal. Job turnover data reflect an uptrend in hiring, but not a strong one. Geopolitical tensions could lead to business caution in the remainder of the year, restraining growth in capital investment and the pace of hiring. The percentage of workers quitting to find new jobs has picked up over the last year, but remains below normal.



Despite a modest uptick in 2Q14 (which followed weather-related weakness in 1Q14), labor compensation has been trending at a lackluster pace, consistent with a high level of slack in the job market. Fed Chair Janet Yellen has indicated a willingness to accept some pick up in average wage income before having to tighten monetary policy.

In short, while the job market has improved significantly this year, it still has a long way to go for a full recovery. Fed policymakers should be willing to let the job market run.

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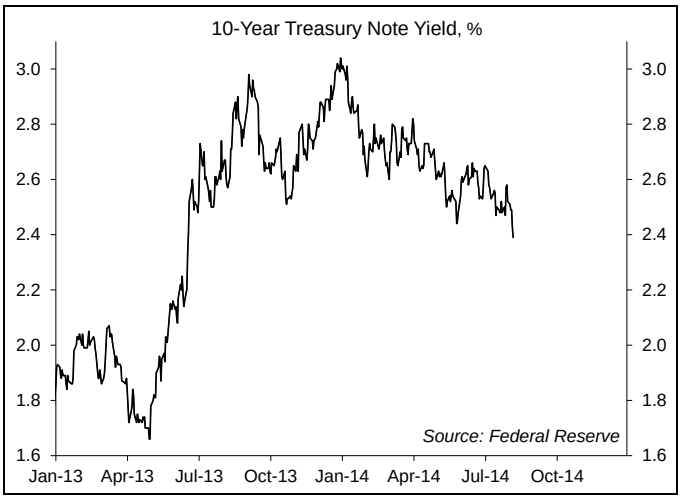
	Treasury Yields								Dollar				Equities		
	13-wk	26-wk	52-wk	2-yr	3-yr	5-yr	10-yr	30-yr	$/Euro	$/BP	JY/$	CD/$	NASD	SPX	DJIA
7/11/14	0.02	0.07	0.11	0.48	0.92	1.65	2.53	3.34	1.360	1.711	101.33	1.072	4415.49	1967.57	16943.81
8/01/14	0.03	0.05	0.13	0.47	0.94	1.67	2.52	3.29	1.344	1.683	102.45	1.092	4352.64	1925.15	16493.37
8/08/14	0.03	0.04	0.09	0.44	0.89	1.62	2.42	3.23	1.341	1.678	102.06	1.097	4371.03	1931.56	16553.93

Recent Economic Data and Outlook

The stock market ignored (mostly positive) earnings reports and the (mostly positive) economic data, focusing instead on geopolitical tensions (Russia/Ukraine, Iraq, Israel/Hamas) and the expected path of Federal Reserve policy. Geopolitical turmoil helped push global bond yields sharply lower.



The ISM **Non-Manufacturing Index** rose to 58.7 in July, vs. 56.0 in June. Details were strong. Business activity picked up. New orders rose at a faster pace. Employment growth improved. Input price pressures were moderate. Comments from supply managers were positive.

The U.S. **Trade Deficit** narrowed to $41.5 billion in June (vs. $44.7 billion in May), lower than assumed in the advance GDP report (implying, all else equal, a small upward revision to the second quarter growth estimate). Merchandise exports edged up 0.1% in June (+2.6% y/y). Merchandise imports slipped 1.4% (+4.7% y/y). Petroleum imports fell 3.3% in June (-6.9% y/y).

Unit Motor Vehicle Sales slowed to a 16.4 million seasonally adjusted annual rate in July, vs. 16.8 million in June and 15.7 million a year earlier.

Factory Orders rose 1.1% in June, up 1.5% y/y. Durable goods orders rose 1.7% (revised from +0.7%), with orders for nondefense capital goods ex-aircraft (NDCGXA) up 3.3% (revised from +1.7%). Shipments of NDCGXA fell 0.3% (vs. -1.0% reported earlier – implying a small upward revision to the second quarter GDP growth estimate).

Wholesale Inventories rose 0.3% in June, while May was revised from +0.5% to +0.3% -- less than assumed in the advance GDP estimate (implying, all else equal, a slight downward revision to the first quarter's growth estimate).

Nonfarm Productivity rose at a 2.5% annual rate in the preliminary estimate for 2Q14 (+1.2% y/y). Output rose at a 5.2% pace (+3.2% y/y), while hours rose at a 2.7% pace (+2.0% y/y). Unit Labor Costs rose at a 0.6% annual rate (+1.9% y/y). Note that these figures can be erratic from quarter to quarter and are subject to large revisions over time.

The **Bank of England**'s Monetary Policy Committee made no changes. The BOE's Inflation Report is due on August 13, while the minutes of the policy meeting are set for August 20.

The **European Central Bank**'s Governing Council left short-term interest rates unchanged and maintained its forward guidance ("the key ECB interest rates will remain at present levels for an extended period of time in view of the current outlook for inflation"). The risks to the growth outlook "remain on the downside," according to ECB President Draghi. Despite low inflation (+0.4% over the 12 months ending in July), the ECB sees risks to the inflation outlook as "limited and broadly balanced." However, "the Governing Council is unanimous in its commitment to also using unconventional instruments within its mandate, should it become necessary to further address risks of too prolonged a period of low inflation."

Economic Outlook (3Q14): 2.5% to 3.0%

Employment: The pace of job growth slowed somewhat in July, following a strong pace in 2Q14. Jobless claims are trending at a low level. Hiring appears to have picked up, but geopolitical risks could be a factor in the months ahead.

Consumers: Real average earnings are trending about flat, but job gains contribute to growth in aggregate wage income, which has helped fuel consumer spending growth.

Manufacturing: Mixed results across industries, but mostly strengthening. Excess inventories and a sluggish global economy are likely to be factors in the remainder of the year.

Housing/Construction: A mixed bag. Affordability issues have weakened demand at the middle level and below. Supply constraints remain an issue for many builders.

Prices: The PCE Price Index, the Fed's chief inflation gauge, picked up in 2Q14, but the year-over-year trend remains well below the Fed's 2% target. Pipeline pressures appear to be mild. Wage pressures are limited. Inflation expectations are steady.

Interest Rates: The tapering of the Fed's monthly pace of asset purchases has continued. Short-term interest rates are expected to remain exceptionally low "for a considerable period" after the asset purchase program ends in late October. The Fed's policy moves in 2015 will be dictated by the evolution of the economic outlook in the second half of 2014.

This Week:					*forecast*	last	last –1	comments
Monday	8/11		no significant data					
Tuesday	8/12	7:30	Small Business Optimism	Jul	***NF***	95.0	96.6	down in June, but trending higher
		10:00	JOLTS: hiring rate	Jun	***NF***	3.4%	3.4%	a very gradual trend of improvement
			JOLTS: quit rate		***NF***	1.8%	1.8%	little changed
		1:00	Treasury Note Auction					$27 billion in 3-year notes
		2:00	Treasury Budget, $bln	Jul	***-96.0***	-97.6	-69.5	an improving trend
Wednesday	8/13	8:30	**Retail Sales**	Jul	***+0.3%***	+0.2%	+0.5%	a lackluster-to-moderate gain
			ex-autos		***+0.4%***	+0.4%	+0.4%	some decrease in gasoline prices
			ex-autos, bld mat, gasoline		***+0.4%***	+0.5%	+0.3%	moderate
		10:00	Business Inventories	Jun	***+0.3%***	+0.5%	+0.6%	lower than assumed in advance GDP est.
		1:00	Treasury Note Auction					$24 billion in 10-year notes
Thursday	8/14	8:30	Jobless Claims, th.	8/09	***299***	289	303	were recent figures distorted?
		8:30	Import Prices	Jul	***NF***	+0.1%	+0.3%	a low trend
			ex-food & fuels		***NF***	-0.1%	+0.1%	no inflation pressure from abroad
		1:00	Treasury Bond Auction					$16 billion in 30-year bonds
Friday	8/15	8:30	**Producer Price Index**	Jul	***+0.2%***	+0.4%	-0.2%	moderate
			ex-food & energy		***+0.1%***	+0.2%	-0.1%	a low trend in core inflation
		8:30	Empire St. Manf. Index	Aug	***16.0***	25.6	19.3	likely to moderate
		9:15	**Industrial Production**	Jul	***+0.3%***	+0.2%	+0.5%	moderate, not especially strong
			Manufacturing Output		***+0.2%***	+0.1%	+0.5%	aggregate hours fell 0.2%
			Capacity Utilization		***79.2%***	79.1%	79.1%	little changed
		9:55	UM Consumer Sentiment	m-Aug	***82.4***	81.8	82.5	range-bound
Next Week:								
Monday	8/18	10:00	Homebuilder Sentiment	Aug	***55***	53	49	recovering
Tuesday	8/19	8:30	**Consumer Price Index**	Jul	***+0.2%***	+0.3%	+0.4%	moderate
			year-over-year		***+2.1%***	+2.1%	+2.1%	little change in y/y pace
			ex-food & energy		***+0.1%***	+0.1%	+0.3%	mild core inflation
			year-over-year		***+1.9%***	+1.9%	+2.0%	a low trend
		8:30	Real Weekly Earnings	Jul	***-0.2%***	0.0%	-0.1%	nominal earnings were essentially flat
		8:30	**Building Permits, th.**	Jul	***1010***	973	1005	reflecting multi-family volatility
			% change		***+3.8***	-3.2	-5.1	moderate strength in single-family
			Housing Starts		***1000***	893	985	likely to rebound sharply
			% change		***+12.0***	-9.3	-7.3	choppy, watch for revisions
Wednesday	8/20	2:00	**FOMC Minutes**	7/30				some insights into endgame outlook
Thursday	8/21	8:30	Jobless Claims, th.	8/16	***307***	***299***	289	a low trend
		9:45	Markit US Manf PMI (flash)	Aug	***NF***	55.8	57.3	not market-moving
		10:00	Philadelphia Fed Index	Aug	***16.2***	23.9	17.8	likely to moderate
		10:00	**Existing Home Sales, mln**	Jul	***5.02***	5.04	4.91	seen little changed
			% change		***-0.4***	+2.6	+5.4	the Pending Home Sales Index slipped
		10:00	Leading Econ Indicators	Jul	***+0.8%***	+0.3%	+0.7%	most components positive
Friday	8/22	tbd	**Yellen Speaks**					at Jackson Hole

This Week…

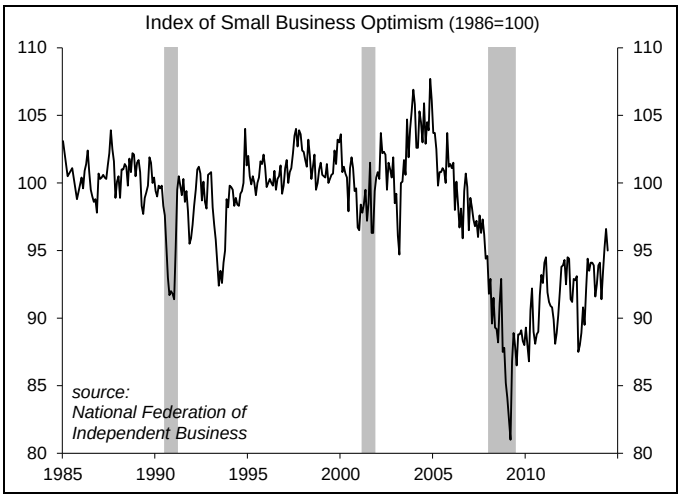
The economic calendar picks up, but the report on retail sales is the only item that should matter for the financial markets (geopolitical tensions will likely remain a dominant factor). Retail sales account for about a third of consumer spending, and consumer spending accounts for 70% of Gross Domestic Product. A key concern is that meager wage growth will restrain consumer spending growth in the second half of the year.

Monday

No significant data.

Tuesday

Small Business Optimism Index (July) – The headline figure fell in June, but that followed a sharp rise in May. The trend is higher, but there have been a number of false starts in the last few years. Geopolitical concerns may not be much of an issue in the July survey, but could be in the months ahead.



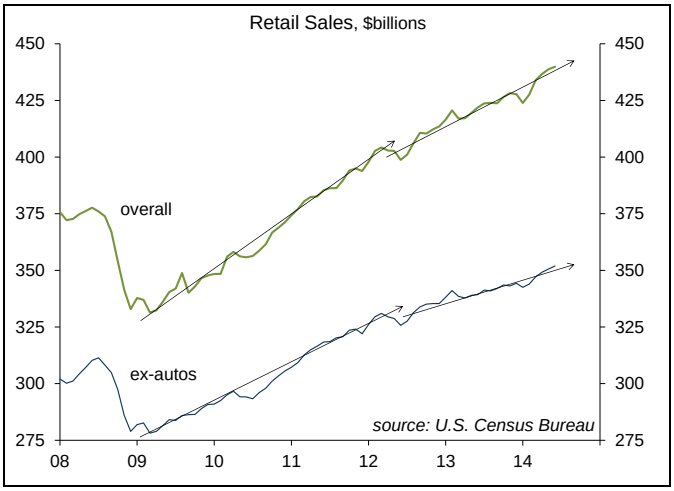
JOLTS Data (July) – Janet Yellen said that hiring and quit rates are on her radar screen. These measures are off the recessionary

lows, but have been trending roughly flat, at a moderate level, over the last several months, suggesting that the job market is still a long way from fully recovered.

Federal Budget (July) – With two months remaining in the fiscal year, the deficit is trending toward 3% of GDP (vs. 9.8% of GDP in FY09). In contrast to the political noise in recent years, this has been a recession story. Tax revenues have rebounded with the economy and should continue to do so as slack is taken up.

Wednesday

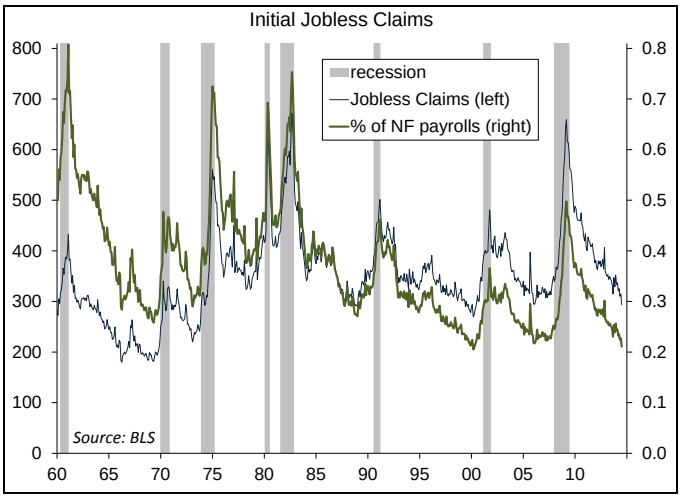
Retail Sales (July) – Unit auto sales edged down last month (although not all sales are to consumers). Weather was a factor earlier this year, but the underlying trend, while positive, does not appear to be especially strong. That likely reflects the weakness in real average earnings.



Business Inventories (June) – The only missing piece here is retail inventories, which were assumed in the advance GDP report to have risen about 0.4% in June.

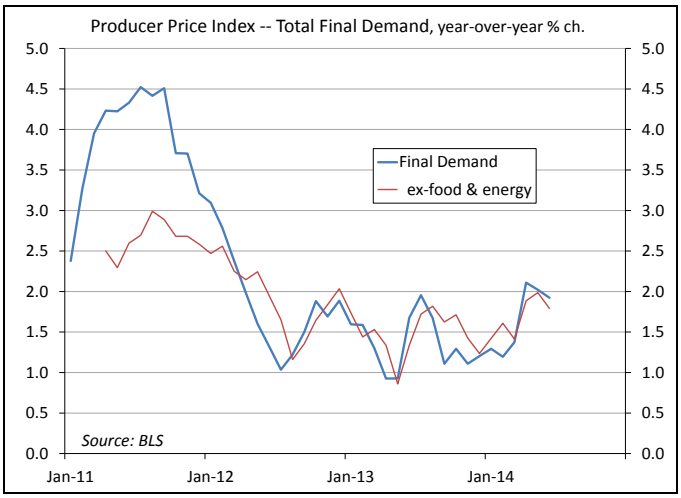
Thursday

Jobless Claims (week ending August 8) – Seasonal adjustment difficulties make the July figure a bit suspect, but the underlying trend had been moving lower in June. Job destruction is low, but that's only part of the overall labor market picture. Hiring has been the key this year, and may be at risk due to geopolitical tensions (that is, firms may become more cautious).

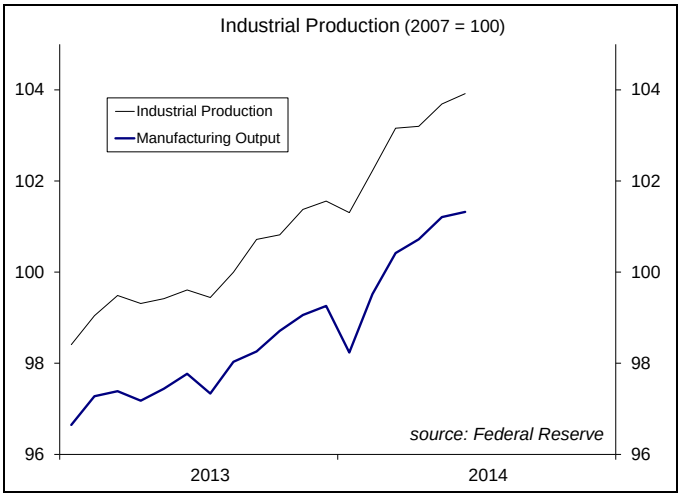


Friday

Producer Price Index (July) – Some minor relief in gasoline prices, but core inflation should remain low.



Industrial Production (July) – Figures for the first half of the year were distorted by bad weather and then the rebound from the weather. The underlying trend appears to be moderate, but aggregate manufacturing hours fell in July.



Next Week …

Waiting on Yellen's Jackson Hole speech.

Coming Events and Data Releases

August 26	Durable Goods Orders (July) Consumer Confidence (August)
August 22	Yellen Jackson Hole Speech
August 28	Real GDP (2Q14, 2nd estimate)
September 1	Labor Day (markets closed)
September 2	ISM Manufacturing Index (August)
September 5	Employment Report (August)
September 17	FOMC Policy Decision, Yellen press conference
October 29	FOMC Policy Decision (no press conference)
December 17	FOMC Policy Decision, Yellen press conference