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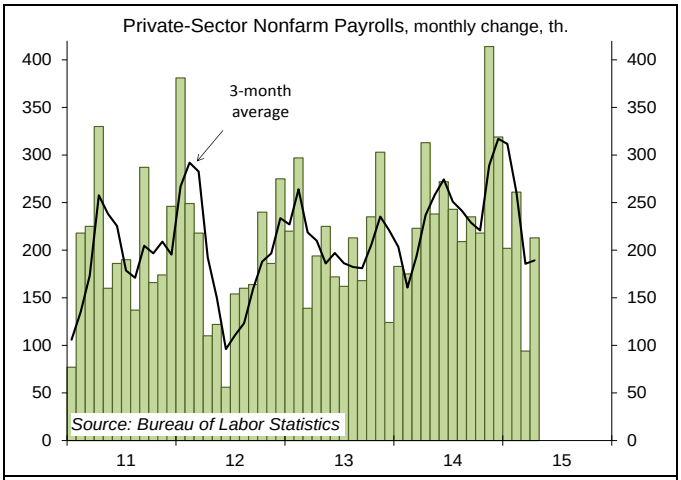
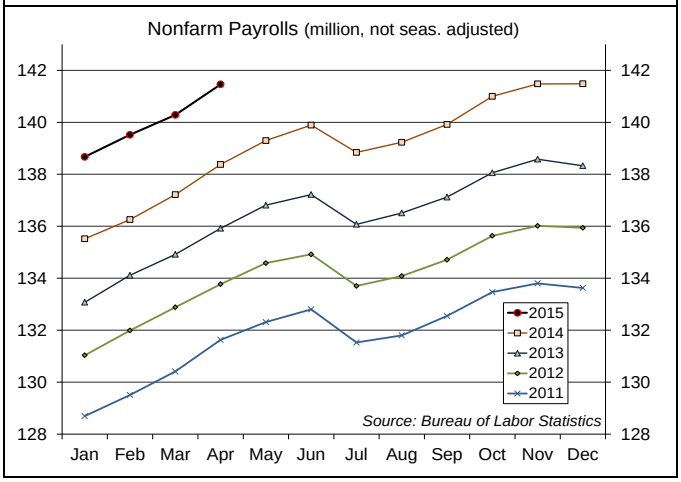
Weekly Market Monitor

In the Market's Sweet Spot

Recent economic data reports have reflected a slowdown in growth, but they are not disastrous. The economy continues to improve, but not so much that the Fed will rush to take away the punch bowl. That's good news for the financial markets.

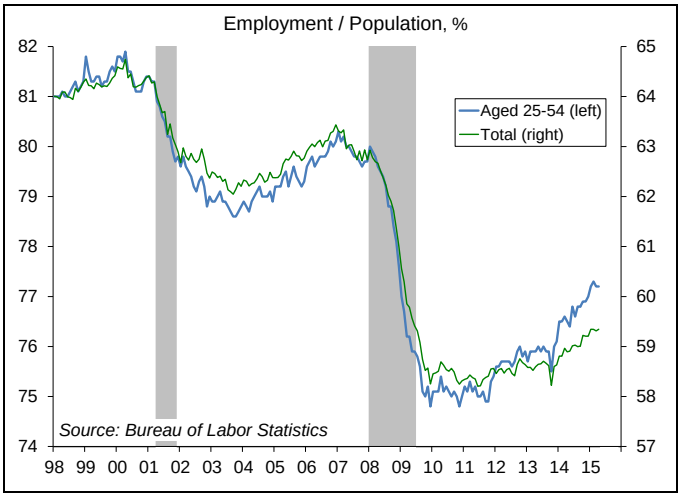
Nonfarm payrolls rose about as expected in the initial estimate for April, but figures for the two previous months were revised down. We know that the subpar payroll figure for March was a weather story. The employment report is made up of two separate surveys, one of establishments and one of households. In February, the establishment survey largely missed the major snowstorms, but bad weather hit the March survey period head on. The household survey details showed a larger-than-usual number of people who could not get to work due to the weather. Granted, the employment report's two surveys are not directly comparable, but they give you a good idea on the weather impact. The April payroll increase largely reflected a rebound from bad weather. The average gain for the two months was 154,000 – a moderate pace.





The unadjusted figures were in line with the usual pattern. The U.S. added 1.178 million jobs in April (before seasonal adjustment), vs. 1.163 million in April 2014. The level of unadjusted payrolls is trending sharply higher relative to a year ago (private-sector jobs are up 2.6% y/y). Still, the underlying trend in seasonally adjusted payrolls has moderated. The ADP estimate shows a sharp slowing in hiring at large firms in March and April, while job gains at small and medium-sized firms have remained relatively strong. This is a contrast to the earlier years of the recovery, when large firms prospered and smaller firms struggled to improve. The gains at small firms are an important signal of a broadening recovery. The softness at larger firms likely reflects the transitional impact of a strong dollar.

For Fed policymakers, the key issue is the amount of slack in the job market. The unemployment rate was 5.4% in April, essentially unchanged from March and down from 6.3% a year ago. However, the employment/population ratio held steady at 59.3%, up only gradually over the last year. Improvement here is more concentrated in the key age cohort (those aged 25-54), but that should broaden to teenagers and young adults over time. Average hourly earnings rose modestly in April, with the year-over-year pace remaining at a lackluster 2.2%. The continued lack of better wage growth is taken as a sign of slack.



The range of recent economic data reports is consistent with a temporary slowdown in growth. The pace should improve as the first quarter's restraining factors (weather, West Coast port delays, the energy contraction, and the stronger dollar) wane, but some restraints have continued into 2Q15. As a consequence, the 2015 economic outlook appears softer and we're back to "more of the same." That is, we're still on the road to economic recovery. We've made a lot of progress, but we're nowhere near where we need to be. The continuation of this backdrop should be taken well by the financial markets.

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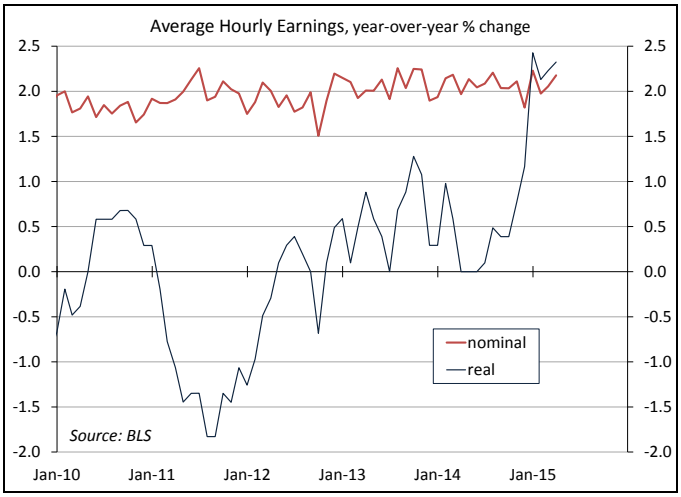
	Treasury Yields								Dollar				Equities		
	13-wk	26-wk	52-wk	2-yr	3-yr	5-yr	10-yr	30-yr	$/Euro	$/BP	JY/$	CD/$	NASD	SPX	DJIA
4/10/15	0.02	0.09	0.24	0.57	0.91	1.41	1.96	2.58	1.060	1.465	120.29	1.260	4995.98	2102.06	18057.65
5/01/15	0.01	0.05	0.25	0.60	0.97	1.50	2.12	2.82	1.119	1.514	120.21	1.219	5005.39	2108.29	18024.00
5/08/15	0.01	0.08	0.23	0.57	0.93	1.49	2.14	2.90	1.121	1.545	119.70	1.209	5003.55	2116.04	18190.65

Recent Economic Data and Outlook

The global bond market sell-off reached a crescendo on Thursday as the 10-year German bund yield spiked to 0.79%, but then quickly fell back below 0.60% (ending the week at about 0.54%). The U.K. election was seen as up for grabs, but the Conservative Party won a surprisingly decisive victory (helping to ease global financial anxieties). Fed Chair Janet Yellen suggested that share prices may be elevated, although this was widely exaggerated by the financial press. The April Employment Report matched market expectations and seemed to keep things in the market's sweet spot. That is, the economy continues to recover, but not so rapidly that the Fed will rush to take the punch bowl away.



The **Employment Report** was about as expected. Nonfarm payrolls rose by 223,000 (median forecast: +225,000), but with a net revision of -39,000 for the two previous months. The unemployment rate was essentially unchanged (5.443%, vs. 5.465% in March), with an increase in labor force participation. Unemployment for teenagers and young adults fell, while the rates for the prime-aged cohort (25-54 years) and older workers edged up. Average weekly hours held steady. Average hourly earnings rose 0.1%, up 2.2% y/y (note the CPI fell 0.1% over the 12 months ending in March). Detail of the report suggest: 1) a rebound from March weather effects; 2) a moderation in the underlying pace of job growth (relative to the brisk pace of 4Q14); and 3) a gradual pace of reduction in labor market slack.

The **ADP Estimate** of private-sector payrolls rose by 169,000 in April, following +175,000 in March. The report showed a sharp slowing in hiring by large firms in the last two months, but continued strength for small and medium-sized firms.

The U.S. **Trade Deficit** widened to $51.4 billion in March, vs. $35.9 billion in February, sharply higher than was assumed in the advance GDP estimate. All else equal, that implies a downward revision to the first quarter growth estimate (now expected to be below zero, vs. a 0.2% annual rate in the advance estimate). While the trade deficit widened moderately in nominal terms in 1Q15 (+1.9% q/q, +4.1% y/y), it rose sharply in real terms (+13.7% q/q, +17.9% y/y).

The **ISM Non-Manufacturing Index** rose to a better-than-expected 57.8 in April, vs. 56.5 in March. Business activity picked up. New orders rose at a faster pace and employment continued to expand at a moderate pace. Comments from supply managers were mixed, but mostly positive.

Nonfarm Labor Productivity fell at a 1.9% annual rate in the preliminary estimate for 1Q15, following a -2.1% pace in 4Q14 (+0.6% y/y). Unit Labor Costs rose at a 5.0% annual rate, vs. +4.2% in 4Q14 +1.1% y/y). Note that productivity figures can be erratic from quarter to quarter and don't necessarily add much to the debate on secular stagnation. However, at face value, the numbers are a bit worrisome (implying upward pressure on inflation or downward pressure on corporate profits).

Asked about the longer-term consequences of very low interest rates, **Fed Chair Janet Yellen** noted that *"equity market valuations at this point are generally quite high."* Many market metrics have suggested that, but the financial press made far too much of the comments, which were taken out of context.

Economic Outlook (2Q15): Around a 2.0% annual rate.

Employment: The pace of job growth slowed, but from an unusually strong pace in 4Q14. Job losses remain very limited. New hiring appears to have remained strong for small and medium-sized firms, but has slowed for larger firms.

Consumers: The drop in gasoline prices from last summer has sharply boosted consumer purchasing power and we should see a pickup in spending in the spring and early summer.

Manufacturing: The stronger dollar is a constraint. A decline in corporate profits has contributed to a softening trend in capital spending. Domestic demand should be picking up.

Housing/Construction: Sales appeared mixed at the start of the spring selling season. Rising prices and relatively tight credit appear to be constraining the lower end of the market.

Prices: The PCE Price Index is about flat year-over-year – and the core inflation rate has moved lower in recent months. Pipeline pressures are mild. Wage pressures are limited. Inflation expectations remain well-anchored.

Interest Rates: Senior Fed officials have signaled that conditions are likely to warrant an initial increase in short-term rates this year, but indicate that the more important question is the pace of tightening after the initial hike (which is likely to be gradual).

This Week:					*forecast*	last	last –1	comments
Monday	5/11	7:00	BOE Policy Decision					no change
Tuesday	5/12	9:00	Small Business Optimism	Apr	***NF***	95.2	98.0	likely to rebound
		10:00	JOLTS: hiring rate	Mar	***NF***	3.5%	3.5%	a gradual trend, but below normal
			JOLTS: quit rate		***NF***	1.9%	2.0%	expecting gradual improvement
		1:00	Treasury Note Auction					$24 billion in 3-year notes
		2:00	Treasury Budget, $bln	Apr	***+155.0***	106.9	112.9	April is a surplus month
Wednesday	5/13	8:30	Import Prices	Apr	***NF***	-0.3%	+0.2%	no pressure
			ex-food & fuels		***NF***	-0.4%	-0.2%	a declining trend
		8:30	**Retail Sales**	Apr	***+0.3%***	+0.9%	-0.5%	moderate
			ex-autos		***+0.5%***	+0.4%	0.0%	moderate
			ex-autos, bld mat, gasoline		***+0.6%***	+0.4%	-0.2%	core sales picking up
		10:00	Business Inventories	Mar	***+0.2%***	+0.2%	-0.0%	assumed up 0.3% in advance GDP est.
		1:00	Treasury Note Auction					$24 billion in 10-year notes
Thursday	5/14	8:30	Jobless Claims, th.	5/09	***278***	265	262	a low trend
		8:30	**Producer Price Index**	Apr	***+0.0%***	+0.2%	-0.5%	seen about flat
			ex-food & energy		***+0.1%***	+0.2%	-0.5%	modest
			ex-f, e, trade services		***+0.1%***	+0.2%	0.0%	a low trend in new core
		1:00	Treasury Bond Auction					$16 billion in 30-year bonds
Friday	5/15	8:30	Empire St. Manf. Index	May	***+6.2***	-1.2	+6.9	erratic, but likely to rebound
		9:15	**Industrial Production**	Apr	***+0.1%***	-0.6%	+0.1%	a lackluster trend
			manufacturing output		***+0.1%***	+0.1%	-0.2%	aggregate hours fell 0.1%
			Capacity Utilization		***78.3%***	78.4%	79.0%	no threat to the inflation outlook
			manufacturing		***77.8%***	77.9%	78.0%	still plenty of excess capacity
		10:00	UM Consumer Sentiment	m-May	***97.0***	95.9	93.0	should pick up a bit
Next Week:								
Monday	5/18	10:00	Homebuilder Sentiment	May	***58***	56	52	likely to improve further
Tuesday	5/19	8:30	**Building Permits, mln**	Apr	***1.085***	1.042	1.102	picking up
			% change		***+4.1***	-5.4	+4.0	single-family strengthening
			Housing Starts		***1.020***	.926	.908	likely to improve
			% change		***+10.2***	+2.0	-15.3	but watch for revisions
Wednesday	5/20	2:00	**FOMC Minutes**	4/29				perhaps a little more insight
Thursday	5/21	8:30	Jobless Claims, th.	5/16	***278***	***280***	265	still low
		10:00	Philadelphia Fed Index	May	***7.0***	7.5	5.0	moderate
		10:00	Existing Home Sales	Apr	***5.30***	5.19	4.89	likely to have improved
			% change		***+2.1***	+6.1	+1.5	better weather may help
		10:00	Leading Economic Indicators	Apr	***+0.5%***	+0.2%	+0.1%	picking up
		1:00	TIPS Auction					10-year TIPS
Friday	5/22	8:30	**Consumer Price Index**	Apr	***+0.2%***	+0.2%	+0.2%	moderate
			year-over-year		***0.0%***	-0.1%	-0.0%	still flat y/y
			ex-food & energy		***+0.2%***	+0.2%	+0.2%	low core inflation
			year-over-year		***+1.8%***	+1.8%	+1.7%	trending higher than core PCE price index
		8:30	Real Hourly Earnings	Apr	***-0.1%***	+0.1%	-0.1%	nominal earnings rose 0.1%
		9:45	Markit US Manf PMI (flash)	May	***NF***	54.1	55.7	not market-moving

This Week…

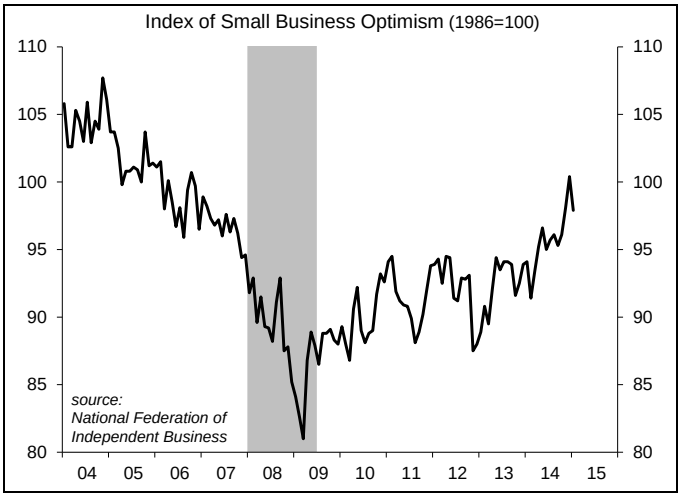
Greece remains on the radar screen and could be a factor on Monday (another kick down the road?). Otherwise, the focus is expected to be on Wednesday's retail sales figures.

Monday

Bank of England Policy Decision – Uneventful. As usual, the BOE does not provide any color when policy is unchanged.

Tuesday

Small Business Optimism Index (April) – The improved outlook has been important to the overall job picture over the last year. However, sentiment softened in March. That may simply reflect the usual noise in the data, but it will be troublesome if we don't see a snap-back in the figures for April.



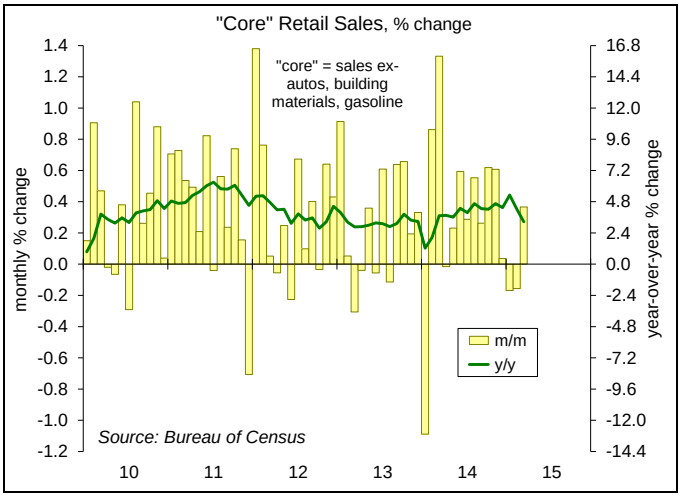
Job Opening and Labor Turnover Survey (March) – The JOLTS data are an important indicator for Fed Chair Yellen. However, these data arrive with a lag and tend to move glacially. Figures through February had suggested that labor market slack is diminishing, but is still far from normal. March figures may be subject to weather-related noise.

Treasury Budget (April) – Tax season means an April surplus and this year's should been higher than a year ago. That should help Treasury dodge the federal debt ceiling for a lot longer.

Wednesday

Import Prices (April) – Oil prices have backed up, but the seasonal adjustment should counter much of that. Import prices have generally be falling over the last year, putting downward pressure on consumer price inflation.

Retail Sales (April) – Unit auto sales fell. Gasoline prices rose. Core sales had been soft in December, January, and February, but finally picked up in March. Retail payrolls posted a lackluster gain in April, suggesting that sales activity may be disappointing. Seasonal adjustment can be a bit tricky.



Business Inventories (March) – The trade deficit was much wider than anticipated in March, implying (all else equal) a downward revision to the estimate of 1Q15 GDP growth. However, some speculated that the wider-than-expected trade gap might be offset by a larger increase in inventories. That doesn't appear to be the case. Manufacturing and wholesale inventories were reported to be slower than was assumed in the advance GDP report. The missing piece is retail inventories (the only new information in this report). Business sales rose 0.4% (-2.3% y/y), outpaced by inventories over the last year.

Thursday

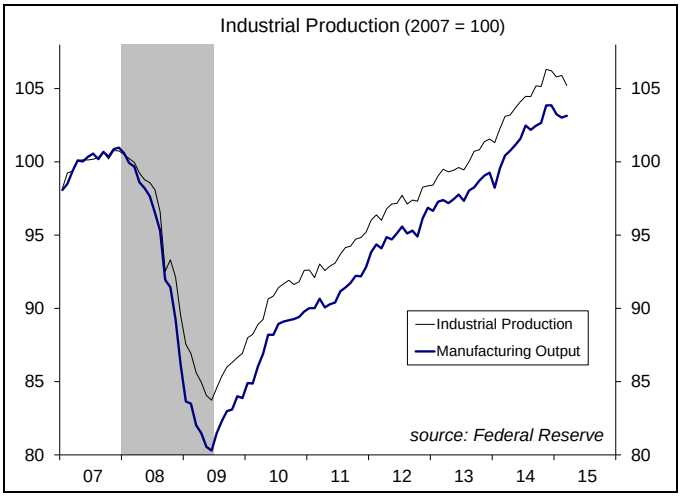
Jobless Claims (week ending May 9) – Figures were a bit uneven in April, but appear to settle down to an exceptionally low pace into early May. However, job losses really aren't an issue.

Producer Price Index (April) – Wholesale gasoline prices rose last month, but the PPI measure will depend on the timing of the data collection and should be largely offset by the seasonal adjustment. Core inflation is expected to remain relatively low. Pipeline pressures should remain mild.

Friday

Empire State Manufacturing Index (May) – The New York Fed's factory sector survey data are often erratic, swinging wildly from month to month. April was relatively soft.

Industrial Production (April) – Aggregate hours (from the Employment Report) fell 0.1% last month, which should be consistent with a mild increase in manufacturing output. Results are likely to be mixed across industries. Capacity utilization should remain at non-threatening levels.



Next Week …

The economic calendar will be less critical for the markets, but we could see reactions to any surprises (relative to expectations). Housing-related figures should reflect a rebound from March's weather. Consumer price inflation is expected to remain relatively low. The minutes of the April 28-29 Fed policy meeting may shed a little more light into the monetary policy outlook (when the Fed will begin to raise rates and how rapidly it goes from there). However, there's some chance that something may be taken out of context, hitting markets one way or another.

Coming Events and Data Releases

May 25	Memorial Day (markets closed)
May 26	Durable Goods Orders (April) Consumer Confidence (May)
May 29	Real GDP (1Q15, 2nd estimate)
June 1	ISM Manufacturing Index (May)
June 3	ECB Policy Decision
June 5	Employment Report (May)
June 17	FOMC Policy Decision, Yellen press conference
July 29	FOMC Policy Decision (no press conference)
September 17	FOMC Policy Decision, Yellen press conference
October 28	FOMC Policy Decision (no press conference)
December 16	FOMC Policy Decision, Yellen press conference