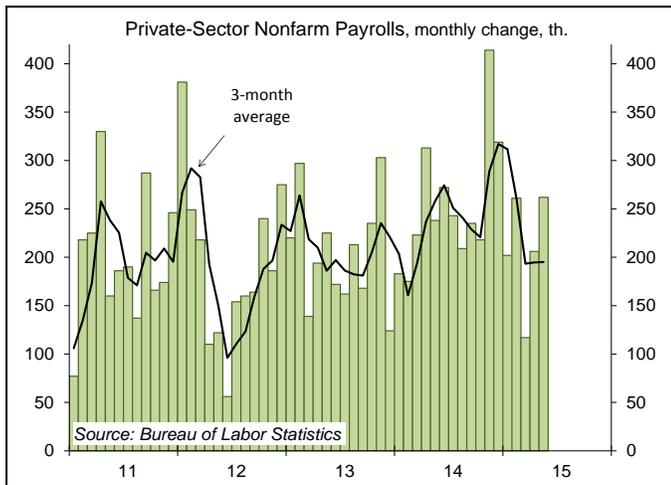


Weekly Economic Monitor

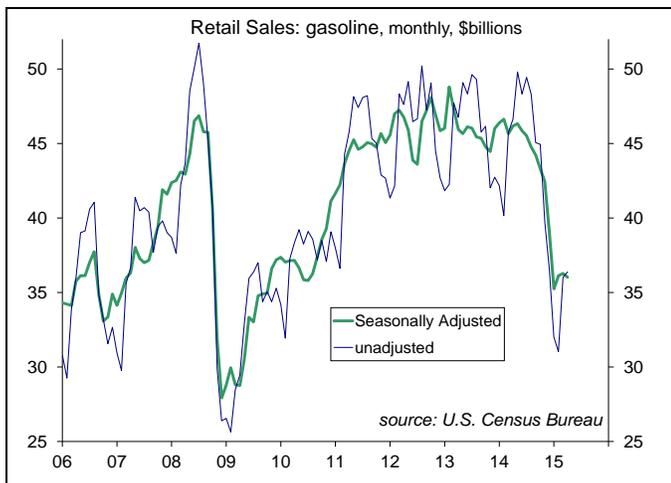
Jobs, Consumer Spending, Gasoline, and the Fed

Job growth was stronger than expected in May, although figures may have been inflated a bit by the seasonal adjustment. Still, the strong job gains over the last year and the drop in gasoline prices have failed to boost consumer spending as anticipated. Following this week's retail sales report, we may better understand why. This may have some impact on the outlook for monetary policy, but Fed officials will want to see a lot more economic data before pulling the trigger.

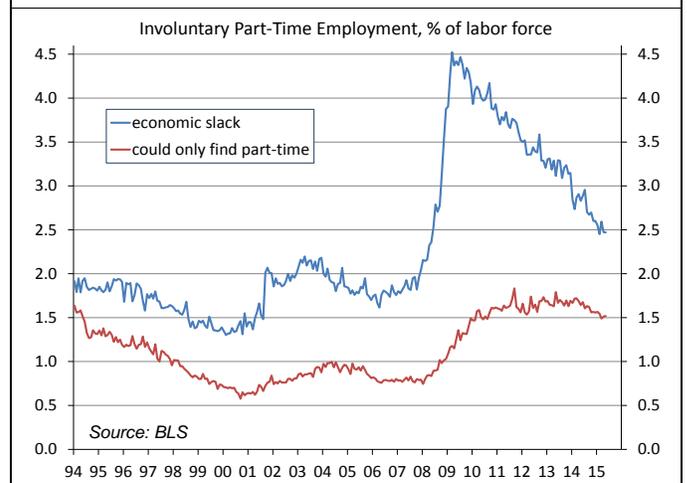
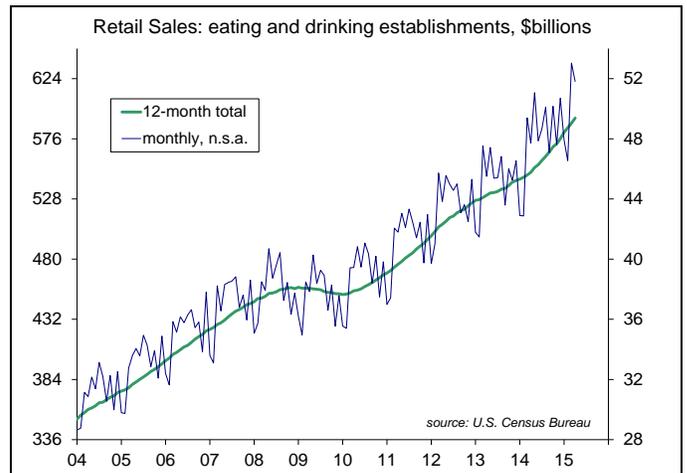


The estimate of nonfarm payrolls, which is subject to statistical noise and seasonal adjustment quirks, is often choppy from month to month. The underlying trend appears to have remained strong through May, although the separate ADP figures continue to suggest a slowing in hiring at large firms.

Consumers have been saving a substantial amount on gasoline expenditures this year. The mystery is why they haven't spent as much of that "savings" as they have in the past. There are a couple of possible explanations.



One possibility is that consumers saw the drop in gasoline prices as temporary, in which case they would be less likely to spend the savings (that's what the economic theory would suggest, although we've never seen much evidence of that historically). Another possibility is that added spending will show up with a lag, especially in the late spring and summer, when consumers generally spend more. It's worth noting that the restaurant component of retail sales rose 9% y/y in the first four months of the year. Recent reports suggest that tourism is doing nicely as the travel season gets underway. Payrolls in leisure and hospitality rose sharply in April and May.



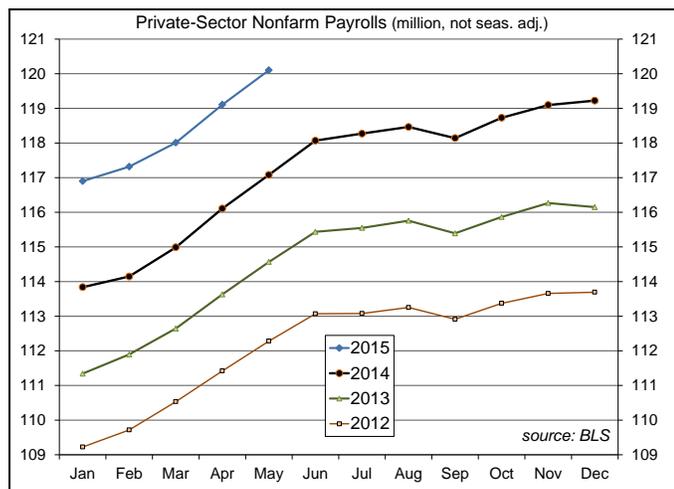
Federal Reserve governors have been clear. Monetary policy moves will be data dependent. Officials want to see further improvement in the job market and be reasonably confident that inflation will move back to the 2% target. There may be liquidity concerns in the bond market and potential turmoil in emerging markets as the Fed begins to tighten – so the Fed will keep a close eye on financial conditions. The pace of tightening after the initial move is expected to be very gradual.

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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	
5/08/15	0.01	0.08	0.23	0.59	0.96	1.50	2.16	2.90	1.124	1.546	119.78	1.209	5003.55	2116.10	18191.11	
5/29/15	0.01	0.06	0.26	0.61	0.94	1.49	2.12	2.88	1.099	1.529	123.98	1.247	5070.03	2107.39	18010.68	
6/05/15	0.02	0.07	0.27	0.72	1.10	1.74	2.40	3.11	1.111	1.527	125.63	1.243	5068.46	2092.83	17849.32	

Recent Economic Data and Outlook

The economic data reports were mixed, but the May payroll figure was stronger than expected, leading to some market adjustment in Fed policy expectations.



The **Fed Beige Book** generally described growth amongst the 12 districts as either “modest” or “moderate.” Employment levels were “up slightly, with some reports of layoffs.” Wages “rose slightly.” Prices were “stable or ticked up.”

The **May Employment Report** was stronger than expected. Nonfarm payrolls rose by 280,000 (median forecast: +225,000), with a net upward revision of +32,000 to March and April. Seasonal adjustment may have been a factor, as unadjusted education jobs fell less than usual. Mining, which includes energy exploration, fell by 17,200, down 68,400 since December. Nonfarm payrolls rose by 3.06 million (2.2%) over the last 12 months. The unemployment rate edged up to 5.5%, reflecting higher labor force participation for teenagers and young adults (which also suggests possible problems with seasonal adjustment). Average weekly hours held steady. Average hourly earnings rose 0.3%, up 2.3% y/y (note that wage figures are often revised in the following month).

Personal Income rose 0.4% in April (+4.1% y/y), with wage and salary income up 0.2% (+4.6% y/y). **Personal Spending** was flat (+2.8% y/y), with gasoline sales down 4.3% (-29.4% y/y). Ex-gasoline, spending rose 0.1% (+4.0% y/y). Adjusted for inflation, spending was also flat, following a 0.4% rise in March (+2.7% y/y). The **PCE Price Index** was unchanged (+0.025% before rounding, +0.1% y/y), up 0.1% ex-food & energy (+1.2% y/y, still a long way from the Fed’s 2% target).

Unit **Motor Vehicle Sales** surged to a 17.7 million seasonally adjusted annual rate in May. However, much of that strength reflects a rebound from a “soft” April (a 16.5 million pace). In addition, the Memorial Day holiday was earlier this year,

effectively creating two weekends of heavy sales promotions (so we could see sales figures fall back in June).

The **ISM Manufacturing Index** rose to 52.8 in May, vs. 51.5 in both March and April. New orders and employment picked up, but production slowed. Input price pressures were flat.

The **ISM Non-Manufacturing Index** fell to 55.7 in May, vs. 57.8 in April and 56.4 in March. Business activity, new orders, and employment continued to advance, but at a somewhat slower pace than in April. Input price pressures picked up slightly.

Factory Orders fell 0.4% in April, reflecting a pullback in aircraft orders. Durable goods orders fell 1.0% (vs. -0.5% in the advance estimate). Orders for nondefense capital goods ex-aircraft fell by 0.3% (vs. +1.0% reported a week earlier).

The U.S. **Trade Deficit** narrowed to \$40.9 billion in April, vs. \$50.6 billion in March. Delays related to labor issues at West Coast ports distorted first quarter trade figures, making it difficult to gauge the impact of a stronger dollar. Adjusted for inflation, the merchandise deficit was relatively close to the first quarter average. Net exports subtracted 1.9 percentage points from 1Q15 GDP growth, the largest quarterly drag since 1985. The April trade figures suggest that net exports may not make much of a contribution (positive or negative) to 2Q15 growth, but that view may change as more information becomes available.

As negotiations on **Greece** appeared to reach an impasse, the IMF said it would allow the country to make payments, due at various points this month, at the end of the month.

Economic Outlook (2Q15): Around a 1.5% to 2.0% annual rate.

Employment: The pace of job growth appears to be relatively strong. Except for energy exploration, job losses are 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 boosted consumer purchasing power, but the pickup in spending has been uneven and less than anticipated.

Manufacturing: The strong 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 believe that conditions are likely to warrant an initial increase in short-term rates this year, but the more important question is the pace of tightening after the initial hike (which is likely to be very gradual).

This Week:				<i>forecast</i>	last	last -1	comments	
Monday	6/08	no significant data						
Tuesday	6/09	9:00	Small Business Optimism	May	NF	96.9	95.2	likely to improve
		10:00	JOLTS: hiring rate (private)	Apr	NF	4.0%	3.9%	trending gradually higher
			JOLTS: quit rate		NF	2.2%	2.2%	still well below normal
			Treasury Note Auction				3-year notes	
Wednesday	6/10	1:00	Treasury Note Auction					re-opened 10-year notes
		2:00	Treasury Budget, \$bln	May	NF	-130.0	-138.7	cumulative trending below 2.5% of GDP
Thursday	6/11	8:30	Jobless Claims, th.	6/06	278	276	284	still subject to seasonal noise
		8:30	Import Prices	May	NF	-0.3%	-0.2%	some pickup in oil prices
			ex-food & fuels		NF	-0.4%	-0.4%	a declining trend
		8:30	Retail Sales	May	+0.9%	0.0%	+1.1%	unit auto sales were sharply higher
			ex-autos		+0.6%	+0.1%	+0.7%	rebounding from soft first quarter
			ex-autos, bld mat, gasoline		+0.5%	+0.1%	+0.6%	moderate (watch for revisions)
		10:00	Business Inventories	Apr	NF	+0.1%	+0.3%	moderate
		12:00	Fed Flow of Funds data					details of 1Q15 credit flows
		1:00	Treasury Bond Auction					re-opened 30-year bonds
Friday	6/12	8:30	Producer Price Index	May	+0.5%	-0.4%	+0.2%	seas. adj. adds to energy price increase
			ex-food & energy		+0.1%	-0.2%	+0.2%	modest "old" core
			ex-f, e, & trade services		+0.1%	+0.1%	+0.2%	modest "new" core
		10:00	Consumer Sentiment	m-Jun	92.0	90.7	95.9	likely to edge a bit higher
Next Week:								
Monday	6/15	8:30	Empire St Manf. Index	Jun	5.4	3.1	-1.2	moderate
		9:15	Industrial Production	May	+0.3%	-0.3%	-0.3%	moderate
			manufacturing output		+0.4%	0.0%	+0.3%	aggregate hours reported up 0.2%
			Capacity Utilization		78.3%	78.2%	78.6%	likely to edge a bit higher
			manufacturing		78.3%	78.0%	78.1%	no threat to the inflation outlook
		10:00	Homebuilder Sentiment	Jun	56	54	56	likely to improve
Tuesday	6/16	8:30	Building Permits, mln	May	1.120	1.140	1.038	single-family strength
			% change			+9.8	-5.5	multi-family volatility
			Housing Starts		1.105	1.135	0.944	a strong trend into 2Q15
			% change			+20.2	+4.9	but watch for revisions
Wednesday	6/17	2:00	FOMC Policy Statement					expecting minor changes in statement
		2:00	Summary of Econ Proj.					dots likely to be a bit lower
		2:30	Yellen Press Briefing					repeating recent themes
Thursday	6/18	8:30	Jobless Claims, th.	6/13	278	278	276	a low trend
		8:30	Consumer Price Index	May	+0.4%	+0.1%	+0.2%	some increase in gasoline prices
			year-over-year		-0.0%	-0.2%	-0.1%	little changed from a year ago
			ex-food & energy		+0.1%	+0.3%	+0.2%	mild core inflation
			year-over-year		+1.8%	+1.8%	+1.8%	a low trend
		8:30	Real Hourly Earnings	May	-0.1%	0.0%	0.0%	nominal earnings rose 0.3%
		8:30	Current Account, \$bln	1Q15	-120.0	-113.5	-98.9	seen wider
10:00	Philadelphia Fed Index	Jun	6.8	6.7	7.5	moderate		
10:00	Leading Econ Indicators	May	+0.3%	+0.7%	+0.4%	mixed components, mostly higher		
		1:00	TIPS Auction				re-opened 30-year TIPS	
Friday	6/19	no significant data						

This Week...

Why haven't consumers spent the windfall from lower gasoline prices? One possible explanation is that the drop in gasoline prices has been seen as temporary (the "savings" less likely to be spent). Gasoline prices have also retraced more than half of the decline. However, increased spending may show up with a lag. The May retail sales report (Thursday) should inform the debate. A lack of important economic news earlier in the week ought to help reduce financial market volatility, but after the retail sales report, attention is expected to turn promptly to the Fed's monetary policy meeting (June 16-17).

Monday

No significant economic data.

Tuesday

Small Business Optimism Index (May) – Attitudes are likely to improve somewhat, although restraints are still apparent.

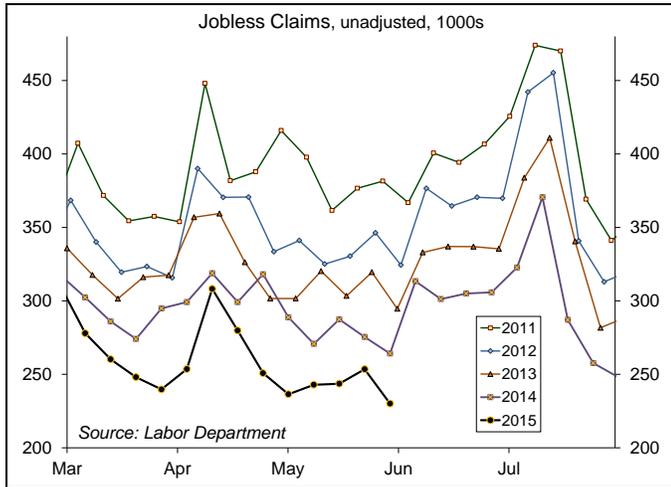
Job Opening and Labor Turnover Survey (April) – Hiring and quit rates are important indirect gauges of labor market slack (according to Fed Chair Yellen), but the figures are somewhat dated and tend to move glacially.

Wednesday

Treasury Budget (May) – The deficit is not a major concern, but we're likely to see the folks in Washington try to make it one. There's a strong chance of a serious showdown over raising the federal debt ceiling later this year.

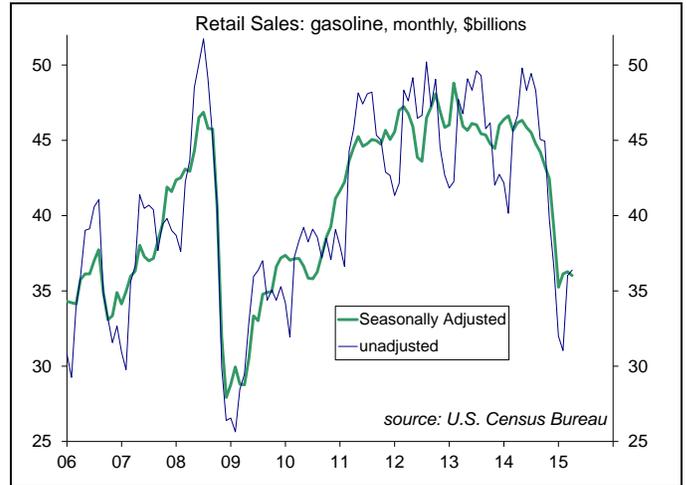
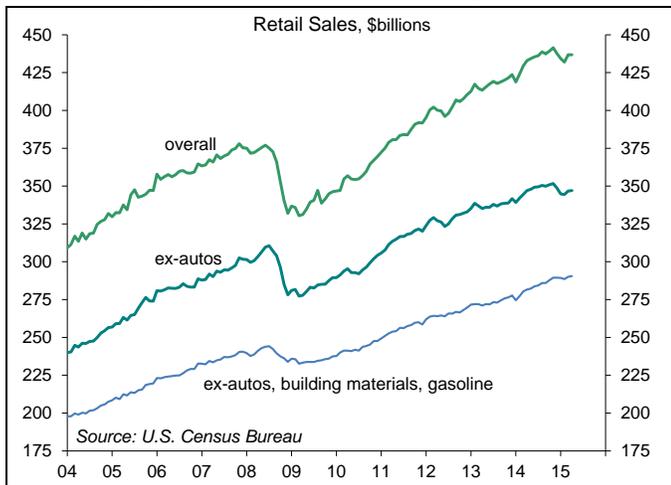
Thursday

Jobless Claims (week ending June 6) – Figures will remain subject to seasonal noise (the rebound from the Memorial Day holiday week and the end of the school year). Take any large swings in the headline figure with a grain of salt. Unadjusted figures have been trending lower than a year ago.



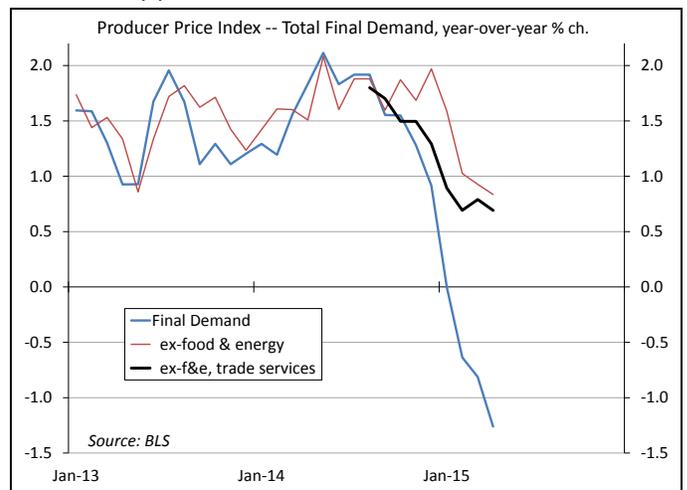
Import Prices (May) – Prices of imported raw materials, intermediate goods, and finished product have generally been falling, reflecting the impact of the strong dollar. We’re unlikely to see much of a reversal anytime soon.

Retail Sales (May) – Unit auto sales were reported sharply higher, but the correlation with retail dealership sales isn’t particularly strong (the unit sales are what’s counted in GDP). Much of that pickup reflects a bounce-back from a soft April. However, vehicle sales depend largely on the last weekend of the month and the early Memorial Day holiday effectively generated two weekends of heavy sales promotions (hence, we could see a letdown in June). Retail trade payrolls rose moderately in May, which is usually a good indicator of overall sales. Gasoline prices rose last month, which ought to add to gasoline sales. Note also that there were five weekends in May. The figures are adjusted for calendar variations (such as the number of weekends), but it’s hard to get it precisely right. In short, this may be a case of bond market bingo.



Friday

Producer Price Index (May) – The Fed is interested in future inflation, not current inflation. The PPI has been suggesting disinflationary pressure.



Next Week ...

The focus will be squarely on the Fed. Officials will revise their economic projections. The dots may drift a bit lower. Fed Chair Yellen is expected to repeat that tightening will likely be gradual.

Coming Events and Data Releases

- June 23 Durable Goods Orders (May)
- June 24 Real GDP (3rd estimate)
- June 30 Consumer Confidence (June)
- July 2 Employment Report (June)
- July 3 Independence Day Holiday (observed)
- July 29 FOMC Policy Decision (no press conference)
- July 30 Real GDP (2Q15 advance, benchmark revisions)
- September 17 FOMC Policy Decision, Yellen press conference
- October 28 FOMC Policy Decision (no press conference)
- December 16 FOMC Policy Decision, Yellen press conference