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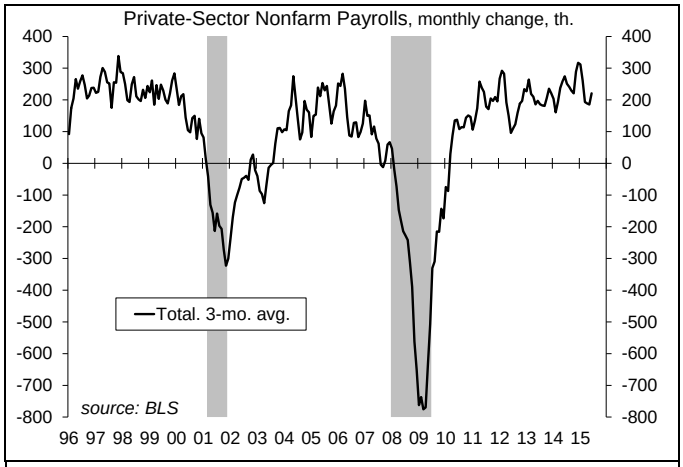
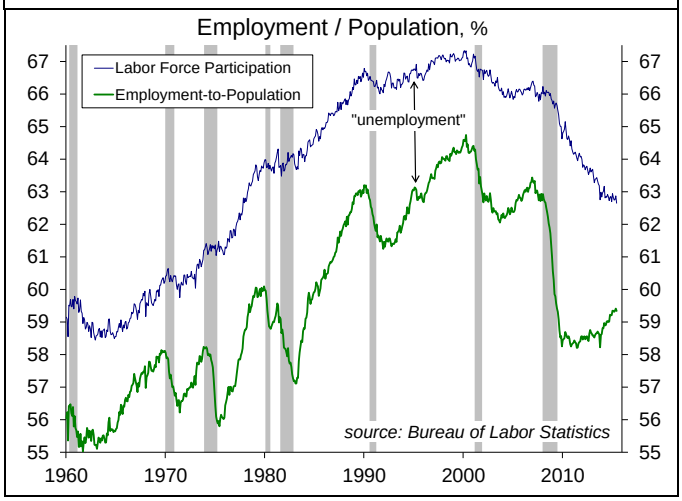
Weekly Market Monitor

More of the Same

The U.S. economic data reports have remained mixed, consistent with a moderately strong pace of growth in the near term. The June jobs data suggest that a September Fed rate hike may be a closer call than thought earlier. Meanwhile, Greece's economy is in tatters. The country has to face the burden of further austerity or the chaos of a euro exit.

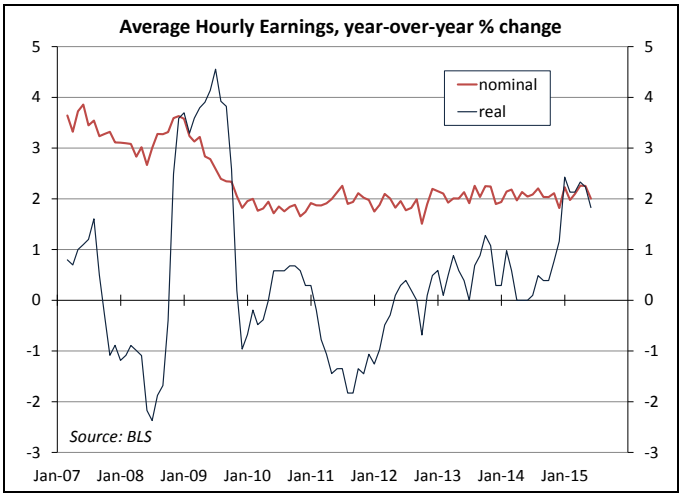
Payrolls rose by 223,000 in June, not far from the median forecast (+230,000), but figures for April and May were revised a net 60,000 lower. At 221,000, the average monthly gain in 2Q15 was still strong, by historical standards.





The unemployment rate dipped to 5.3% in June, the lowest since April 2008. However, the decline was due to a further drop in labor force participation, the lowest since 1977. That's likely just noise (statistic uncertainty and seasonal adjustment issues), but the employment/population ratio suggests that a considerable amount of slack remains in the labor market. Slack is being taken up, but (despite strong job growth over the last year) we are still a long way from a full recovery in employment.

The job market outlook will be a key factor in the Fed's decision to begin raising short-term interest rates. Policymakers have also signaled that they need to be "reasonably confident" that inflation will move toward the 2% goal (core inflation, as measured by the PCE Price Index, rose 1.2% for the 12 months ending in May). Wage growth is the key issue in both of these policy triggers. Reduced labor market slack should eventually lead to wage pressures and, barring a rise in productivity growth, higher labor costs are likely to be eventually passed along to consumers. Last month, average hourly earnings were reported to have risen by 0.3% in May, generating some fear the rising wage pressures would force the Fed to begin tightening sooner rather than later. In contrast, the June jobs report showed earnings unchanged in June, while the May increase was revised down to +0.2%. That left nominal earnings up 2.0% for a year ago, the same lackluster pace of the last few years.



The Fed need not wait for "the white of inflation's eyes" before raising rates. Monetary policy is based on where officials expect the economy to be in a year. Chair Yellen has noted that policy will still be "very accommodative" even after the first couple of hikes. On the other hand, the risks aren't symmetric. Tightening too soon would be more costly than moving too late. However, the more important question is the pace of tightening beyond the initial hike. That pace is expected to be gradual, but it could be made even more measured if the economy were to stumble or grow more slowly than anticipated.

Greece votes on July 5 whether to accept further austerity conditions, but it's unclear what will happen regardless of the outcome. "Yes" would mean a new government, new negotiations, and further uncertainty. "No" would likely lead to an exit from the monetary union, but that's not entirely clear. Greece's economy is going to suffer either way and global financial markets are likely to remain stressed in the near term.

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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
6/05/15	0.03	0.08	0.29	0.73	1.13	1.75	2.41	3.11	1.111	1.527	125.58	1.249	5068.46	2092.83	17849.46
6/26/15	0.01	0.08	0.29	0.72	1.09	1.75	2.49	3.25	1.116	1.574	123.92	1.236	4484.28	2101.49	17946.68
7/02/15	0.01	0.10	0.25	0.64	0.99	1.64	2.39	3.19	1.109	1.561	123.04	1.254	4433.39	2076.67	17729.08

Recent Economic Data and Outlook

Once again, financial market participants' views on Greece shifted from optimism to pessimism, from confusion to, well, even more confusion. Greece decided to have a referendum (July 5) on whether to accept the bailout conditions proposed by the Institutions (the European Commission, the European Central Bank, and the International Monetary Fund). The country missed a scheduled June 30 payment to the IMF (which considers Greece to be "in arrears" rather than "in default"). Greek Prime Minister Tsipras wrote that the country was "prepared to accept" a deal with small modifications, and then went on TV to urge citizens to vote "no." European leaders said there would be no further negotiations until after the vote. U.S. data reports were mixed, but generally consistent with an improving economic outlook.

The June **Employment Report** was not quite as strong as anticipated, but was still relatively good. Nonfarm payrolls rose by 223,000, just under the median forecast (+230,000), but the two previous months were revised a net 60,000 lower. Private-sector payrolls also rose by 223,000, a 221,000 month average for 2Q15. The unemployment rate fell to 5.3% (from 5.5%), but that was due to a drop in labor force participation (to 62.6%, from 62.9%). Don't read too much into that, as the data are subject to statistical noise and seasonal adjustment can be tricky in June (due to the end of the school year). Average hourly earnings were unchanged, following a 0.2% increase in May (revised from +0.3%), up a lackluster 2.0% year-over-year.

Motor Vehicle Sales fell back to a 17.1 million seasonally adjusted annual rate in June, matching the average of the two previous months (17.7 million in May and 16.5 million in April). The pace was stronger than in 1Q15, suggesting that vehicles will make a moderate contribution to 2Q15 GDP growth.

The Conference Board's **Consumer Confidence Index** rose to 101.4 in June, vs. 84.6 in May. Current job market perceptions were less pessimistic and respondents turned optimistic about future job availability. Expectations of household income were little changed. Results were mixed across regions.

The **ISM Manufacturing Index** rose 53.5 in June, vs. 52.8 in May and 51.5 in April. New orders improved, production continued to advanced, and employment growth picked up. Export orders fell modestly. Input price pressures remained soft. Comments from supply managers were mixed, but generally positive.

Factory Orders fell 1.0% in May, down 6.3% y/y. Durable goods orders were revised to -2.2% (from -1.8%), with April down 1.7% (revised from -1.5%), down 3.1% from a year earlier. Orders for nondefense capital goods fell 0.4% (vs. +0.4% reported in the advance estimate), down 2.1% y/y.

Construction Spending rose 0.8% in May (+8,2% y/y). For the private sector, residential spending rose 0.3% (+7.8% y/y) – at a pace roughly even with that of 1Q15. Nonresidential rose 1.5% (+12.7% y/y) – a significant pickup relative to the first quarter. Public construction spending rose 0.7% (+2.8% y/y).

The **Pending Home Sales Index** rose 0.9% in May, up 10.4% y/y. Results varied by region (+6.3% in the Northeast, -0.6% in the Midwest, -0.8% in the South, and +2.2% in the West).

Economic Outlook (2Q15): Around a 2.5% annual rate.

Employment: The pace of job growth, while slower than in the second half of 2014, still appears to be relatively strong. Job losses are very limited. New hiring appears to have remained strong, especially for small and medium-sized firms.

Consumers: Strong job growth is supportive. Inflation-adjusted wages have been trending gradually lower since January, but are still up significantly from a year ago. Consumers are more optimistic about the economy, but generally remain judicious in how they spend their money.

Manufacturing: The strong dollar has been a constraint, but likely a transitory one (assuming the dollar stabilizes). A decline in corporate profits has contributed to a softening trend in capital spending. Domestic demand should be picking up.

Housing/Construction: An improving outlook, although the recovery has remained disappointing. Job growth is supportive and mortgage rates remain low. However, credit is still tight at 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 later this year, but the more important question is the pace of tightening after the initial hike (which is expected to be very gradual). Long-term rates should trend gradually higher.

This Week:					*forecast*	last	last –1	comments
Monday	7/06	10:00	**ISM Non-Manf. Index**	Jun	***56.0***	55.7	57.8	moderate
Tuesday	7/07	8:30	**Trade Balance, $bln**	May	***-43.0***	-40.9	-50.6	seen wider
			goods only		***-62.7***	-60.7	-70.0	some increase in oil prices
		10:00	JOLTS: hiring rate	May	***NF***	3.5%	3.6%	lower in April, but a gradual trend higher
			JOLTS: quit rate		***NF***	1.9%	2.0%	still below normal
		1:00	Treasury Note Auction					$24 billion in 3-year notes
Wednesday	7/08	1:00	Treasury Note Auction					$21 billion in re-opened 10-year notes
		2:00	**FOMC Minutes**					looking for clues on timing and pace
Thursday	7/09	8:30	Jobless Claims, th.	7/04	***278***	281	271	holiday adjustment adds uncertainty
		1:00	Treasury Bond Auction					$13 billion in re-opened 30-year bonds
Friday	7/10	12:30	**Fed Chair Yellen Speaks**					*"U.S. Economic Outlook"*
Next Week:								
Monday	7/13	2:00	Treasury Budget, $bln	Jun	***NF***	+70.5	+116.5	June is a surplus month
Tuesday	7/14	8:30	Import Prices	Jun	***NF***	+1.3%	-0.2%	more modest pressure in oil
			ex-food & fuels		***NF***	0.0%	-0.3%	a low trend in recent months
		8:30	**Retail Sales**	Jun	***+0.3%***	+1.2%	+0.2%	vehicle sales fell back from strong May
			ex-autos		***+0.6%***	+1.0%	+0.1%	some push from higher gasoline prices
			ex-autos, bld mat, gasoline		***+0.5%***	+0.6%	+0.3%	moderately strong
		9:00	Small Business Optimism	Jun	***NF***	98.3	96.9	should be trending higher
		10:00	Business Inventories	May	***NF***	+0.4%	+0.1%	likely to be lower
Wednesday	7/15	8:30	**Producer Price Index**	Jun	***+0.3%***	+0.5%	-0.4%	some boost from food and gasoline
			ex-food & energy		***+0.1%***	+0.1%	-0.2%	mild (old) core inflation
			ex-f, e, trade services		***+0.2%***	-0.1%	+0.1%	mild (new) core inflation
		8:30	Empire St. Manf. Index	Jul	***+4.2***	-2.0	3.1	likely to pick up
		9:15	**Industrial Production**	Jun	***+0.1%***	-0.2%	-0.5%	soft
			manufacturing		***0.0%***	-0.2%	+0.1%	aggregate hours fell 0.2%
			Capacity Utilization		***78.0%***	78.1%	78.3%	no threat to the inflation outlook
			manufacturing		***77.6%***	77.8%	78.0%	well below the long-term trend
		10:00	**Yellen Mon Pol Testimony**					to House Financial Services Committee
		2:00	Fed Beige Book					still "mixed" to "moderate" across regions?
Thursday	7/16	7:45	ECB Policy Decision					Draghi on QE, Greece, etc.
		8:30	Jobless Claims, th.	7/11	***276***	***278***	281	still subject to seasonal noise
		10:00	Philadelphia Fed Index	Jul	***14.0***	15.2	6.7	moderate
		10:00	Homebuilder Sentiment	Jul	***60***	59	54	trending higher
		2:30	**Yellen Monetary Policy**					to Senate Banking Committee
Friday	7/17	8:30	**Consumer Price Index**	Jun	***+0.3%***	+0.4%	+0.1%	some minor boost from gasoline
			year-over-year		***+0.2%***	+0.0%	-0.2%	still close to 0% y/y
			ex-food & energy		***+0.1%***	+0.1%	+0.3%	mild core inflation
			year-over-year		***+1.7%***	+1.7%	+1.8%	roughly steady
		8:30	Real Hourly Earnings	Jun	***-0.3%***	-0.1%	0.0%	nominal earnings were flat
		8:30	**Building Permit, mln**	Jun	***1.070***	1.250	1.140	multi-family pulled forward into May
			% change		***-14.4***	+9.6	+9.8	continued strength in single-family
			Housing Starts		***1.145***	1.036	1.165	volatility in multi-family
			% change		***+10.5***	-11.1	+22.1	choppy, but improving trend in single-fam
		10:00	UM Consumer Sentiment	m-Jul	***97.2***	96.1	90.7	likely to improve further

This Week…

Greece. Markets will begin the week by reacting to Sunday's referendum result (the vote is whether to accept the Institutions' demands), but it's unclear what happens next. If, as expected, the "yes" vote prevails, negotiations can begin again, but where that will lead is anyone's guess. There is some haste to reach, at the very least, a temporary agreement to carry things through the summer (in other words, let's just kick the can down the road on more time). If "no" wins, that would seem to pave the way for an exit from the euro, but not necessarily. In short, there's a strong chance the uncertainty over Greece is not going to disappear completely. On Friday, Fed Chair Janet Yellen will speak on the U.S. economic outlook.

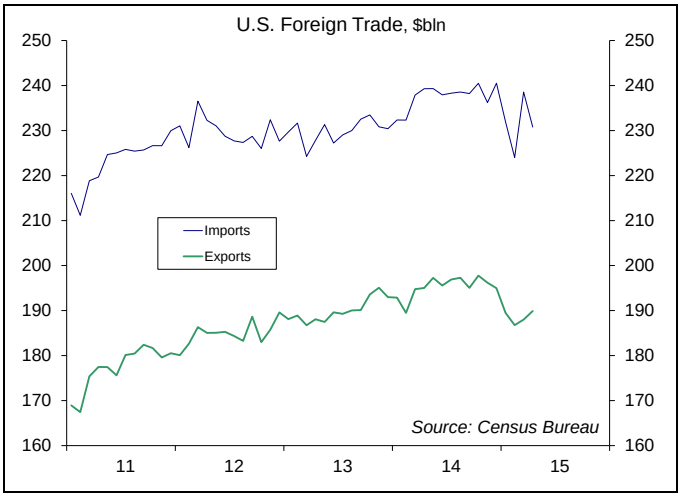
Monday

ISM Non-Manufacturing Index (June) – The ISM's "other" survey is likely to remain consistent with moderate growth in the overall economy. Comments in May suggested some variation across industries, but new orders and business inventories should continue to advance at a relatively strong pace.

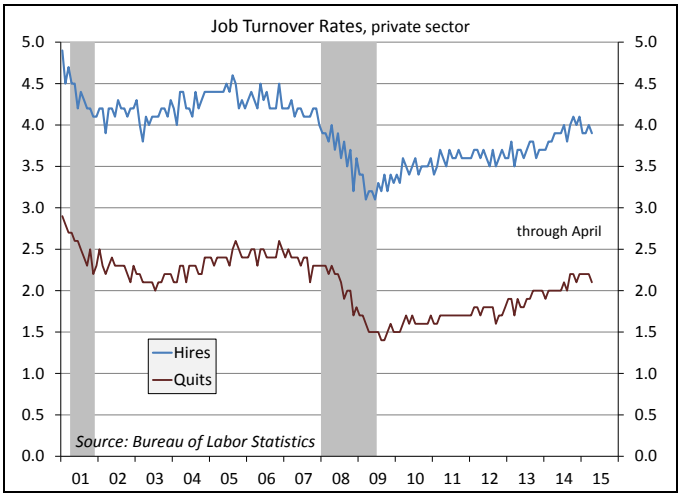
Tuesday

Trade Deficit (May) – Trade figures are normally choppy, but this year has been especially erratic, reflecting the impact of a strong dollar and West Coast port delays. Exporters continue to report that the dollar is a drag, but the data are likely to suggest a possible leveling out. Imports are likely to trend higher

(reflecting the dollar and strength in the domestic economy) and the bounce in crude oil prices. Note that the Bureau of Census will begin issuing an "advance" trade report later this month (July 30), which will include goods only. The report will precede the full trade release by a week.



Job Opening and Labor Turnover Survey (May) – Fed Chair Yellen highlighted hiring and quit rates as important gauges of the labor market's strength. These figures have been trending gradually higher (with a fair amount of chop from month to month), but they suggest the recovery is far from complete.

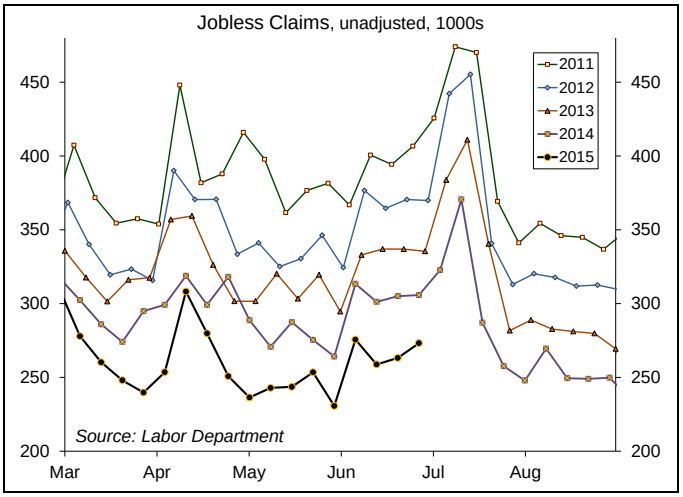


Wednesday

FOMC Minutes (June 16-17) – Following the release of the Fed's revised economic projections and Yellen's post-FOMC press conference, there's unlikely to be any new information in the meeting minutes. However, we may be able to gauge the range of opinions on monetary policy. There's some chance that the financial markets may take something out of context, but the Fed is getting better at preventing misunderstandings and the markets have gotten better at ignoring the noise.

Thursday

Jobless Claims (week ending July 5) – There are two factors that are likely to distort the data in early July. One is that there is usually some catch-up in the states' reporting to the Labor Department (corrections arrive at the start of the next quarter). The other is the seasonal plant retooling shutdowns in the auto industry. A couple of decades ago, plant layoffs were spread over the summer, but they became increasingly concentrated in early July (to coincide with the model-year changeover). So, it wouldn't be surprising to see some volatility in the adjusted claims figures over the next few weeks.



Friday

Fed Chair Yellen Speech ("The U.S. Economic Outlook") – While the markets may see this speech as a preview of next week's monetary policy testimony (July 15 and 16), Yellen is not expected to cover new ground here. Following some transitory restraints in the first part of the year, the economy is expected to pick up steam. The key takeaway should be that the Fed sees the economy as on track to warrant an initial rate hike later this year (most likely at the September FOMC meeting).

Next Week …

The calendar looks like an interstate pile-up (but, hopefully, without all the carnage and loss of property). In four days we'll get the June reports for retail sales, industrial production, producer prices, consumer prices, and residential construction. But wait, there's more. Fed Chair Yellen will deliver her semi-annual monetary policy to Congress. This testimony is less important than it used to be (back when the Fed was less communicative), but investors will want to tune in anyway.

Coming Events and Data Releases

July 22	Existing Home Sales (June)
July 24	New Home Sales (June)
July 27	Durable Goods Orders (June)
July 29	FOMC Policy Decision (no press conference)
July 30	Real GDP (2Q15 advance, benchmark revisions)
August 7	Employment Report (July)
September 17	FOMC Policy Decision, Yellen press conference
October 28	FOMC Policy Decision (no press conference)
December 16	FOMC Policy Decision, Yellen press conference