

U.S. Outlook

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Date	Indicator	For	Estimate	Consensus*	Previous Period
13-Sep-2016	NFIB Small Business Optimism	Aug	94.8	94.8	94.6
14-Sep-2016	Import Price Index MoM	Aug	-0.1%	-0.1%	0.1%
15-Sep-2016	Current Account Balance	2Q	-\$119.0b	-\$119.8b	-\$124.7b
15-Sep-2016	Retail Sales Advance MoM	Aug	-0.1%	-0.1%	0.0%
15-Sep-2016	Retail Sales Ex Auto MoM	Aug	0.2%	0.3%	-0.3%
15-Sep-2016	Initial Jobless Claims	10-Sep	263K	NA	259K
15-Sep-2016	Philadelphia Fed Business Outlook	Sep	0.0	1.0	2.0
15-Sep-2016	PPI Final Demand MoM	Aug	0.1%	0.1%	-0.4%
15-Sep-2016	PPI Ex Food and Energy MoM	Aug	0.1%	0.1%	-0.3%
15-Sep-2016	Empire Manufacturing	Sep	-1.0	-1.0	-4.21
15-Sep-2016	Industrial Production MoM	Aug	-0.3%	-0.2%	0.7%
15-Sep-2016	Capacity Utilization	Aug	75.7%	75.7%	75.9%
15-Sep-2016	Business Inventories	Jul	0.1%	0.1%	0.2%
16-Sep-2016	CPI MoM	Aug	0.1%	0.1%	0.0%
16-Sep-2016	CPI Ex Food and Energy MoM	Aug	0.2%	0.2%	0.1%
16-Sep-2016	U. of Mich. Sentiment	Sep P	91.6	91.0	89.8
16-Sep-2016	Household Change in Net Worth	2Q	NA	NA	\$837b

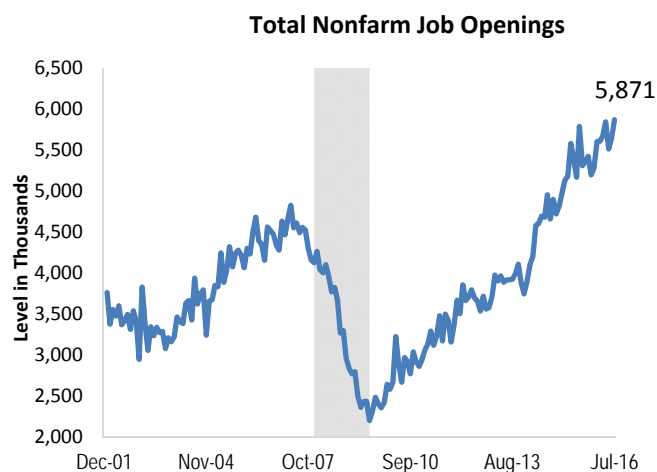
*Consensus from Bloomberg

September FOMC Rate Hike- A Go or No Go?

Several prominent Fed governors have tried in recent weeks to prepare markets for a near-term 0.25 percentage point rate hike, citing a robust labor market and the approach of full-employment as reasons to start lifting rates again. Job openings hit a new record high of 5.875 million in July, and initial claims were at an exceptionally low 259K last week with the 4-week average dropping to a lean 261K.

In the next breath, they talk about a lower neutral Fed funds rate than we have seen in the past. The neutral Fed funds rate is a policy rate that neither accelerates price inflation nor stifles it. This rhetoric suggests another scaling-back of median FOMC rate hike expectations for 2017 and 2018 in the “dot-plot” that gets released along with the September FOMC Meeting.

Job Openings At New Record Highs in July

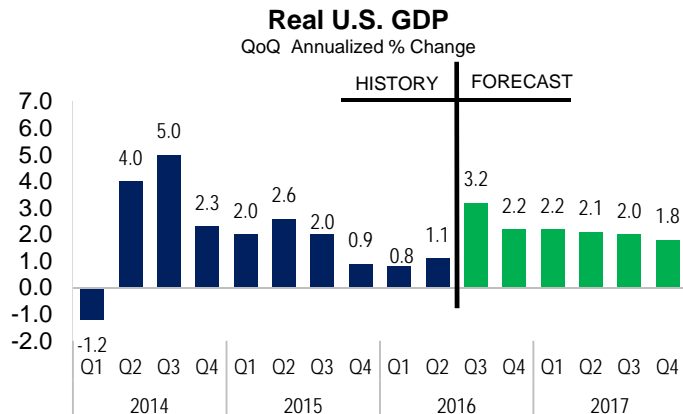


Source: U.S. Bureau of Labor Statistics

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Janet Yellen gave her two cents at the Fed's annual Jackson Hole meeting stating that "the case for interest rate hikes has strengthened". Indeed, the much-feared financial contagion from the U.K. Brexit vote has been more limited than expected so far, and early indications are U.S. GDP growth is bouncing back in the current quarter.

A Solid Q3 Bounce- Then What Comes Next?

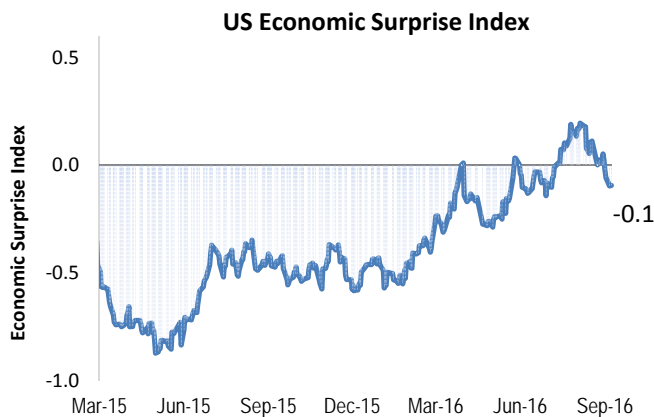


Source: Bureau of Economic Analysis, BOTW Economics

With all that said, we believe another rate hike from the FOMC at their September 21st meeting would be a risky policy move and premature. Here's why.

There are already growing signs the U.S. economy may be cooling down in August into September. The U.S. economic surprise index has turned negative again over the past month, indicating that several indicators have recently underwhelmed analyst expectations. Just in the last two weeks, August payrolls, ISM Manufacturing and Service Indexes, vehicle sales, and the Labor Market Conditions Index have all missed consensus analyst expectations.

August Data is Generally Falling Short of Expectations



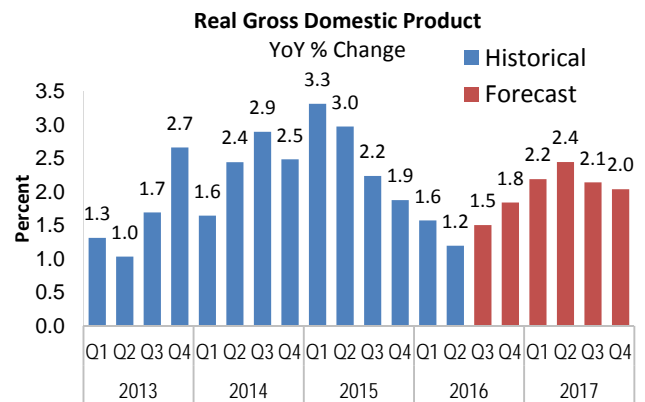
Source: Bloomberg

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The near-term Brexit risk is behind us, but the U.S. election risk is right in front of us. The latest Beige Book from the Fed, an anecdotal report on current economic conditions was not a thrilling read. The Beige Book stated the U.S. economy was growing modestly, but with signs of slowing in some Fed districts and there are a few ominous references to the fact that the upcoming national election could already be dampening the real estate outlook. Bottom-line, the summer bounce the U.S. economy got in June and July may be short-lived.

Even with the bounce in GDP growth expected in the third quarter, it is important to take stock of where we are. The trend in U.S. GDP growth has been slower not faster growth over the past year and a half. GDP growth has been just 1.2% year-on-year through the second quarter down from 3.3% in the first quarter of 2015. Moreover, our outlook for growth does not give any reason to rush interest rates higher in September. A better case could be made to raise rates in December in our view.

A Solid Q3 Bounce- Then What Comes Next?



Source: Bureau of Economic Analysis; BOTW Economics

Finally, the financial markets are not expecting a rate hike in September. According to Bloomberg, Fed funds futures markets are placing only a 38% probability of a Fed rate hike in September. The probability of the next rate hike occurring at the December meeting rises to 63%. The FOMC does not want to surprise markets and in the past has liked these probabilities to be between 80% and 100%, before they raise rates. In short, a September rate hike from the Fed appears to be a high-bar to clear.

Major Economic Indicators

Economic Data	History						Forecast						Yr/Yr % chg or Annual Avg.			
	2015.1	2015.2	2015.3	2015.4	2016.1	2016.2	2016.3	2016.4	2017.1	2017.2	2017.3	2017.4	2014	2015	2016	2017
Real GDP*	2.0	2.6	2.0	0.9	0.8	1.1	3.2	2.2	2.2	2.1	2.0	1.8	2.4	2.7	1.5	2.2
Personal Consumption Expenditures*	2.4	2.9	2.7	2.3	1.6	4.4	3.4	2.8	2.5	2.5	2.4	2.3	2.7	3.1	2.8	2.8
Non-residential Fixed Investment*	1.3	1.6	3.9	-3.3	-3.4	-0.9	2.6	2.0	2.7	2.8	2.9	2.8	6.2	2.4	-0.7	2.4
Private Housing Starts (000s units)	986	1,156	1,156	1,135	1,151	1,156	1,200	1,220	1,240	1,250	1,280	1,300	1,001	1,108	1,182	1,268
Vehicle Sales (mill. Units, annualized)	16.9	17.2	17.7	17.8	17.2	17.1	17.0	17.1	17.0	17.0	16.9	16.9	16.4	17.4	17.1	17.0
Industrial Production*	-1.9	-2.7	1.5	-3.3	-1.7	-0.8	1.9	1.8	1.7	1.8	1.7	1.7	3.7	-0.5	-0.8	1.6
Nonfarm Payroll Employment (mil.)	140.8	141.5	142.2	142.9	143.5	144.0	144.5	145.0	145.5	146.0	146.6	147.1	138.9	141.8	144.3	146.3
Unemployment rate	5.6	5.4	5.2	5.0	4.9	4.9	4.8	4.7	4.6	4.6	4.6	4.5	6.2	5.3	4.8	4.6
Consumer Price Index* (percent)	-2.9	2.4	1.4	0.8	-0.3	2.5	2.0	2.1	2.2	2.2	2.3	2.3	1.6	0.1	1.2	2.2
"Core" CPI* (percent)	1.7	2.3	1.8	2.2	2.7	2.1	1.9	2.0	2.0	2.0	2.1	2.1	1.7	1.8	2.2	2.0
PPI (finished goods)* (percent)	-11.0	3.4	-0.4	-4.8	-5.3	3.6	2.1	2.5	2.4	2.2	2.0	2.0	1.9	-3.3	-1.0	2.4
Trade Weighted Dollar (Fed BOG, major)	89.3	90.1	91.7	93.1	93.3	89.6	90.2	91.7	92.0	92.5	92.0	91.6	78.4	91.1	91.2	92.0
Crude Oil Prices -WTI (\$ per barrel)	48	58	46	42	33	45	45	47	47	47	48	49	93	49	43	48

*Quarterly Data Percent Change At Annual Rate; Annual Data Year-on-Year % Chg, or Annual Average.

Financial Data	History						Forecast						Annual Average			
	2015.1	2015.2	2015.3	2015.4	2016.1	2016.2	2016.3	2016.4	2017.1	2017.2	2017.3	2017.4	2014	2015	2016	2017
S & P 500	2,064	2,102	2,027	2,052	1,951	2,075							1,930	2,061		
Dow Jones Industrial Average	17,808	18,004	17,077	17,475	16,663	17,764							16,770	17,591		
Federal Funds Rate (effective)	0.11	0.13	0.13	0.16	0.36	0.37	0.41	0.46	0.63	0.63	0.88	0.96	0.09	0.13	0.40	0.77
Treasury-3 Month Bills (yield)	0.02	0.02	0.04	0.13	0.29	0.26	0.30	0.35	0.53	0.53	0.80	0.88	0.03	0.05	0.30	0.69
Treasury-2 Year Notes (yield)	0.60	0.61	0.69	0.84	0.84	0.77	0.71	0.80	1.04	1.06	1.31	1.41	0.46	0.69	0.78	1.21
Treasury-5 Year Notes (yield)	1.46	1.53	1.56	1.58	1.37	1.24	1.11	1.20	1.49	1.57	1.77	1.87	1.64	1.53	1.23	1.68
Treasury-10 Year Notes (yield)	1.97	2.16	2.22	2.19	1.91	1.75	1.54	1.75	2.02	2.17	2.32	2.47	2.54	2.14	1.74	2.25
Treasury-30 Year Notes (yield)	2.55	2.88	2.96	2.96	2.72	2.57	2.24	2.50	2.77	2.92	3.12	3.32	3.34	2.84	2.51	3.03
Prime Rate	3.25	3.25	3.25	3.29	3.50	3.50	3.50	3.58	3.75	3.75	4.00	4.08	3.25	3.26	3.52	3.90
Libor 3-Mo. U.S. Dollar	0.30	0.30	0.33	0.43	0.67	0.65	0.77	0.85	0.94	0.95	1.17	1.25	0.25	0.34	0.74	1.08
Mortgage-30 Year (yield)	3.72	3.82	3.95	3.90	3.74	3.59	3.45	3.59	3.86	4.01	4.16	4.31	4.17	3.85	3.59	4.09
BAA Corporate (yield)	4.50	4.83	5.24	5.42	5.30	4.66	4.22	4.50	4.80	4.96	5.17	5.45	4.85	5.00	4.67	5.10

Source: Bank of the West Economics, Bloomberg, Federal Reserve