BANK OF THE WEST
BNP PARIBAS

U.S. Outlook

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Date	Indicator	For	Estimate	Consensus*	Previous Period
5-Sep-2017	Factory Orders	Jul	-3.5%	-3.2%	3.0%
6-Sep-2017	Trade Balance	Jul	-$44.4b	-$44.5b	-$43.6b
6-Sep-2017	Markit US Services PMI	Aug F	57.0	NA	56.9
6-Sep-2017	Markit US Composite PMI	Aug F	NA	NA	56.0
6-Sep-2017	ISM Non-Manufacturing Composite	Aug	55.0	55.1	53.9
6-Sep-2017	U.S. Federal Reserve Releases Beige Book				
7-Sep-2017	Initial Jobless Claims	02-Sep	242k	NA	236k
7-Sep-2017	Nonfarm Productivity	2Q F	1.1%	1.0%	0.9%
7-Sep-2017	Unit Labor Costs	2Q F	0.6%	0.6%	0.6%
8-Sep-2017	Wholesale Inventories MoM	Jul F	0.4%	0.4%	0.4%
8-Sep-2017	Consumer Credit	Jul	$14.50b	$15.00b	$12.40b

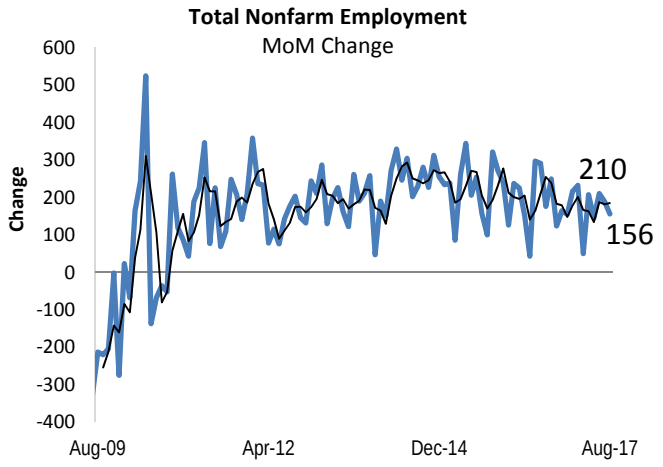
*Consensus from Bloomberg

Job Report Increases Doubts about Fed Rate Hike Path

The August jobs report came in on the weak side pretty much across the board, raising concerns that with core consumer inflation running well below the Fed's 2.0% target and no sign yet of accelerating wages, the Fed's gradual tightening path could become glacial in the year ahead — especially if the Fed goes ahead with its balance sheet normalization plan in September.

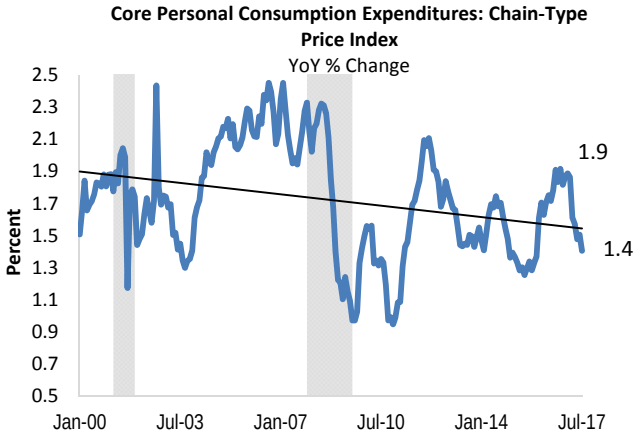
Here's what could keep the Fed on hold more than it would like next year: Core inflation, i.e., inflation excluding volatile food and energy categories, isn't budging. The July personal income and spending report released this week showed another month of weak consumer price inflation. The Fed's preferred measure of core inflation, the PCE deflator, held at a low 1.4% y-o-y in July. Back in March when the FOMC laid out its rate hike path expectations through 2018, the core PCE deflator already stood at 1.9%.

August Job Gains Underwhelm



Source: U.S. Bureau of Labor Statistics

Core Inflation Continues on its Downtrend Through July



Source: U.S. Bureau of Economic Analysis

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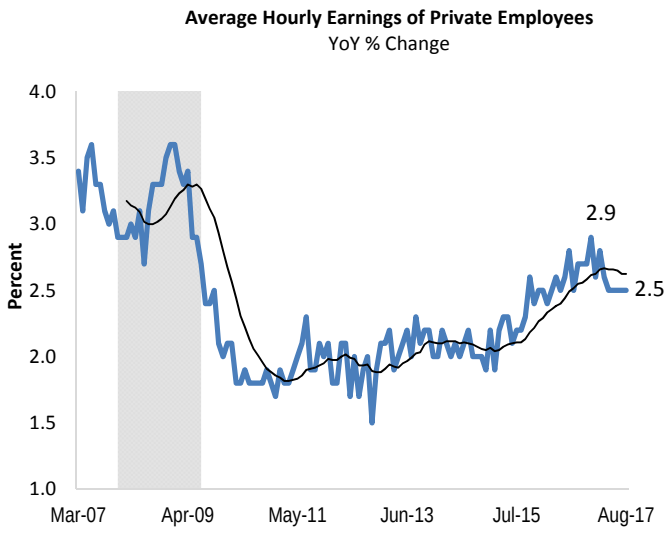
Moreover, with average hourly earnings growth of only 0.1% last month and 2.5% over the past year, and the U.S. unemployment rate rising last month back up to 4.4%, there is little fear that an overheating labor market will stoke faster consumer inflation anytime soon. Our forecast doesn't have core PCE inflation y-o-y exceeding the Fed's 2.0% target for more than three months until Q4 2019.

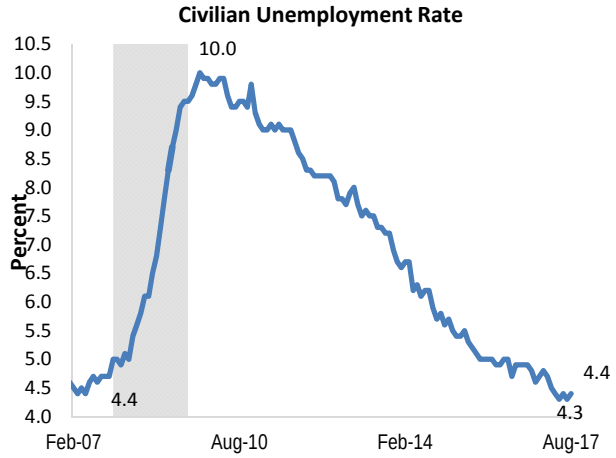
Average Hourly Earnings Growth Momentum Fades



Source: Bureau of Labor Statistics

The increase in the U.S. unemployment rate to 4.4% in August is perhaps the most discouraging data point from this morning's release.

Unemployment Rises on August Household Employment Drop

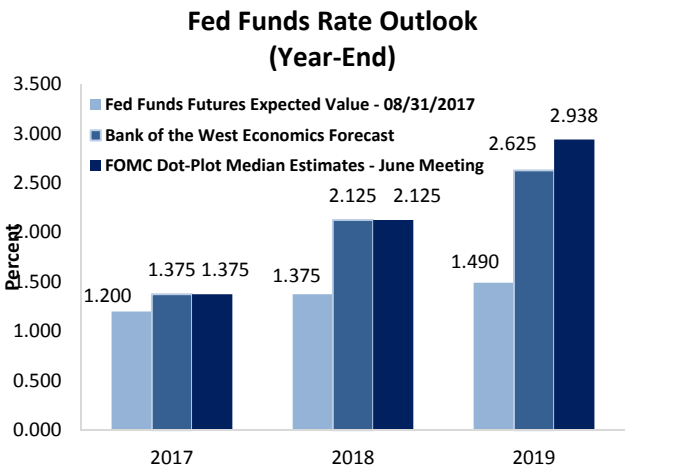


Source: U.S. Bureau of Labor Statistics

The increase in the unemployment rate was driven by an outright decline in monthly household employment of 74K jobs, not a huge jump in the labor force like sometimes happens when more folks return to the labor market. In other words the increase in the unemployment rate wasn't driven by labor market strength, but due to new labor market weakness.

According to the latest Fed dot-plot, the median FOMC expectation is for one more quarter-point rate hike in December and three more quarter-point moves in 2018 and 2019. A comparison of Fed funds rate expectations at year-end 2017, 2018, and 2019 show how far off the FOMC's forecasts are compared to the Fed funds futures market current expectations. Unfortunately, the August payroll report only serves to further muddy the waters, and should further increase doubt in the FOMC's forecast for three additional rate hikes next year.

Doubts about Fed Rate Hike Path Solidifying



Source: Chicago Board of Trade: Federal Reserve: Bank of the West

We have not yet changed our view on three Fed rate hikes for 2018, but we do have more sympathy for the wait-and-see approach this morning. The September jobs numbers will not add much clarity either, since we expect Hurricane Harvey to reap havoc on the payroll numbers and further cloud the economic outlook. There will only likely be a month or maybe two of cleaner economic indicators before the FOMC will have to make a decision about another rate hike at its December meeting.

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Major Economic Indicators

	History				Forecast								Yr/Yr % chg or Annual Avg.			
Economic Data	**2016.1**	**2016.2**	**2016.3**	**2016.4**	**2017.1**	**2017.2**	**2017.3**	**2017.4**	**2018.1**	**2018.2**	**2018.3**	**2018.4**	**2015**	**2016**	**2017**	**2018**
Real GDP*	0.6	2.2	2.8	1.8	1.2	3.0	3.0	2.2	2.0	2.1	2.1	2.1	2.6	1.5	2.2	2.3
Personal Consumption Expenditures*	1.8	3.8	2.8	2.9	1.9	3.3	2.8	2.4	2.2	2.2	2.1	2.1	3.2	2.7	2.7	2.4
Non-residential Fixed Investment*	-4.0	3.3	3.4	0.2	7.2	6.9	4.4	2.8	2.8	3.4	3.9	4.4	2.1	-0.6	4.5	3.6
Private Housing Starts (000s units)	1,153	1,158	1,150	1,248	1,238	1,165	1,230	1,256	1,263	1,265	1,275	1,285	1,108	1,177	1,222	1,272
Vehicle Sales (mill. Units, annualized)	17.3	17.2	17.5	17.8	17.1	16.8	16.8	16.8	16.7	16.6	16.6	16.5	17.4	17.5	16.9	16.6
Industrial Production*	-1.3	-0.7	0.8	0.7	1.6	5.2	1.8	1.9	2.2	2.3	2.2	2.2	0.3	-1.2	1.9	2.3
Nonfarm Payroll Employment (mil.)	143.4	144.0	144.7	145.2	145.7	146.2	146.7	147.2	147.7	148.2	148.7	149.2	141.8	144.3	146.5	148.4
Unemployment rate	4.9	4.9	4.9	4.7	4.7	4.4	4.3	4.2	4.2	4.1	4.2	4.3	5.3	4.9	4.4	4.2
Consumer Price Index* (percent)	0.1	2.3	1.8	3.0	3.1	-0.3	1.9	2.2	2.2	2.0	2.0	2.0	0.1	1.3	2.0	1.9
"Core" CPI* (percent)	2.5	2.1	2.1	2.0	2.5	0.6	1.9	2.0	2.1	2.1	2.1	2.1	1.8	2.2	1.9	2.0
PPI (finished goods)* (percent)	-3.9	3.0	1.7	3.4	6.3	0.4	3.2	2.8	2.1	1.8	1.6	1.6	-3.3	-1.0	3.3	2.1
Trade Weighted Dollar (Fed BOG, major)	93.2	89.5	90.3	93.5	94.5	93.1	89.0	89.7	90.2	90.5	90.2	90.0	90.9	91.6	91.6	90.2
Crude Oil Prices -WTI ($ per barrel)	33	45	45	49	52	48	47	48	49	49	50	50	50	43	49	50

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

	History				Forecast								Annual Average			
Financial Data	**2016.1**	**2016.2**	**2016.3**	**2016.4**	**2017.1**	**2017.2**	**2017.3**	**2017.4**	**2018.1**	**2018.2**	**2018.3**	**2018.4**	**2015**	**2016**	**2017**	**2018**
S & P 500	1,951	2,075	2,162	2,185	2,326	2,398							2,061	2,093		
Dow Jones Industrial Average	16,663	17,764	18,372	18,865	20,406	20,994							17,591	17,916		
Federal Funds Rate (effective)	0.36	0.37	0.39	0.45	0.70	0.94	1.15	1.21	1.46	1.71	1.96	2.13	0.13	0.39	1.00	1.81
Treasury-3 Month Bills (yield)	0.29	0.26	0.30	0.43	0.61	0.91	1.03	1.10	1.36	1.63	1.90	2.07	0.05	0.32	0.91	1.74
Treasury-2 Year Notes (yield)	0.84	0.77	0.73	1.01	1.24	1.30	1.33	1.50	1.75	2.06	2.30	2.48	0.69	0.84	1.34	2.15
Treasury-5 Year Notes (yield)	1.37	1.24	1.13	1.61	1.95	1.81	1.82	2.00	2.30	2.52	2.72	2.98	1.53	1.34	1.90	2.63
Treasury-10 Year Notes (yield)	1.91	1.75	1.56	2.14	2.45	2.26	2.28	2.50	2.77	3.00	3.26	3.45	2.14	1.84	2.37	3.12
Treasury-30 Year Notes (yield)	2.72	2.57	2.28	2.83	3.05	2.90	2.88	3.10	3.37	3.62	3.90	4.05	2.84	2.60	2.98	3.74
Prime Rate	3.50	3.50	3.50	3.55	3.80	4.05	4.25	4.30	4.55	4.80	5.00	5.25	3.26	3.51	4.10	4.90
Libor 3-Mo. U.S. Dollar	0.62	0.64	0.79	0.92	1.07	1.21	1.31	1.40	1.66	1.92	2.17	2.35	0.34	0.74	1.25	2.03
Mortgage-30 Year (yield)	3.74	3.59	3.45	3.84	4.17	3.98	3.95	4.18	4.45	4.72	4.98	5.18	3.85	3.66	4.07	4.83
BAA Corporate (yield)	5.30	4.66	4.26	4.64	4.66	4.49	4.35	4.65	5.03	5.25	5.52	5.78	5.00	4.71	4.54	5.40

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