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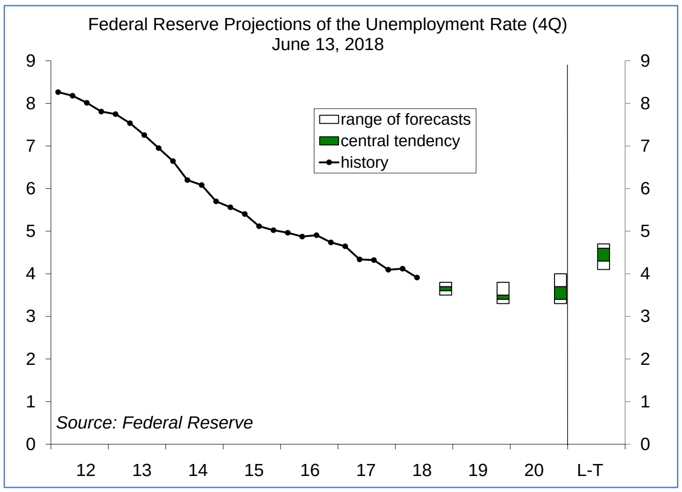
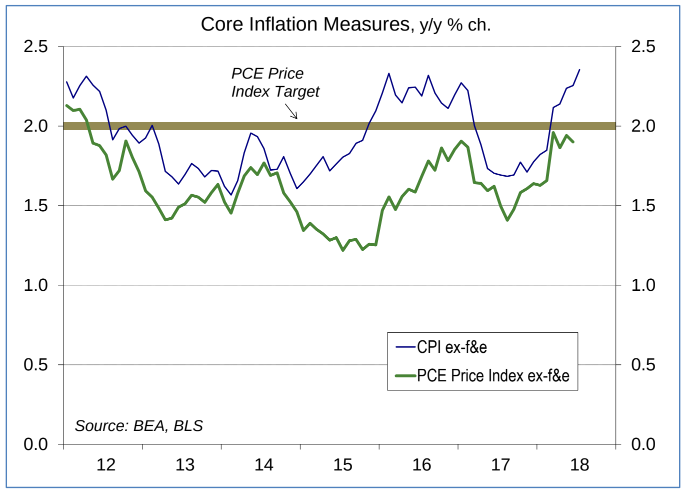
Weekly Economic Monitor

Powell at Fed Camp – The Kansas City Fed's annual monetary policy symposium begins later this week in Jackson Hole, Wyoming. Around 120 people attend the conference, including central bankers from around the world. In the past, the Fed chair's speech has often been a big deal for the financial markets. This will be Powell's first speech as Fed chair and the title (*"Monetary Policy in a Changing Economy"*) suggests the possibility of a change in the Fed's approach or some modification in its thinking. However, whether Powell provides any new clues is an open question. Of greater interest will be the debates and discussions (the impact of trade policy uncertainty, full employment) in the hallways and around the grounds. Powell may even address these issues.

There were a few oddities in the June 13 Summary of Economic Projections (forecasts of senior Fed officials). The unemployment rate was expected to fall a bit further, averaging 3.6% in 4Q18 and 3.5% in both 4Q19 and 4Q20. However, the long-term average was seen as 4.3-4.6%, which implies that the economy would have to slow below its potential (the Fed sees the longer-term average of GDP growth at 1.8-2.0%). Job growth has remained relatively strong this year, well beyond a long-term sustainable pace (based on the demographics). At the same time, while wage growth has picked up, the pace is not especially strong (well below the kind of appreciation we've seen around low unemployment rates in the past). In hindsight, there was more slack in the job market than many had expected, but that slack is still declining. Labor costs are the widest channel for inflation pressure.





Inflation, as measured by the PCE Price Index excluding food and energy, is expected to match the Fed's 2% goal for the 12 months ending in July (data due August 30). Fed officials have indicated a tolerance for having core inflation trend a bit above the 2% goal for a while. In this way, 2% becomes a target, rather than a ceiling (and in turn, inflation expectations should be anchored at 2%, rather than a bit below – that's important for the Fed). With the exception of oil, commodity price pressures are not a major inflationary concern. It takes a gigantic increase in the prices of raw materials to have much of an impact at the consumer level. Increased tariffs have raised prices in some sectors (washing machines up 20%, lumber adding $9,000 to the average price of a new home), but have not been a significant factor in boosting overall inflation – at least, so far. However, the University of Michigan's survey of consumer sentiment noted that recent data suggest that "consumers have become much more sensitive to even relatively low inflation rates than in past decades" and tariff concerns appear to have weakened buying perceptions for autos and new homes in early August (these are two of the most cyclically sensitive components of the economy).

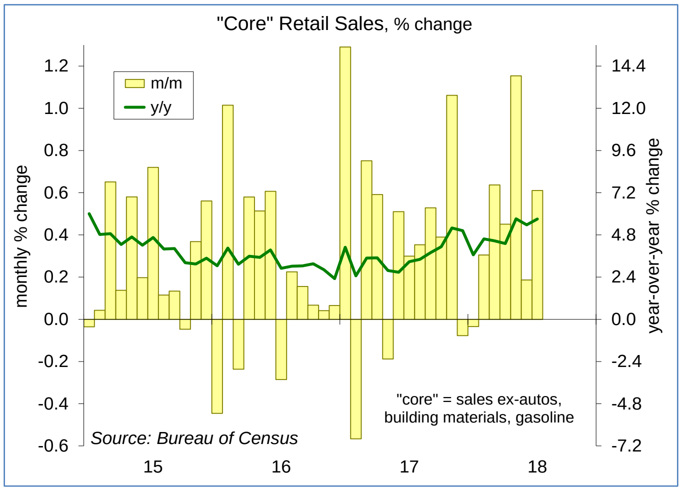
The direct economic impact of increased tariffs may be limited, although that depends on how long the trade war lasts and how far it escalates. The indirect effects may be more troublesome and the long-term consequences can be severe. Trade policy uncertainty is a dampening factor for capital investment at home and abroad. Emerging market economies have improved with global trade. Pulling away from global trade leaves the U.S. at a disadvantage as these countries develop their own internal demand, including an appetite for U.S. exports (especially in services) – this has been really short-sighted.

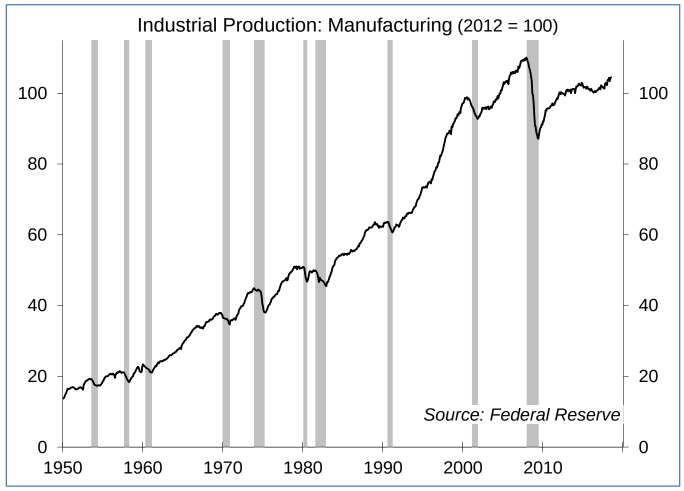
Judging by the federal funds futures market, it's still full steam ahead for a September 26 Fed rate hike. However, with monetary policy close to neutral, it's likely that the Fed will consider a pause at some point. Markets believe that the Federal Open Market Committee will only act at meetings where there is a press conference. That's not the true, but we won't have to worry about that for much longer. There will be a press conference after every FOMC meeting beginning next year.

	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
7/20/18	1.99	2.16	2.41	2.60	2.68	2.77	2.89	3.03	1.171	1.311	111.74	1.316	7820.20	2801.83	25058.12
8/10/18	2.05	2.23	2.42	2.61	2.68	2.75	2.87	3.03	1.140	1.277	110.66	1.313	7839.11	2833.28	25313.14
8/17/18	2.04	2.23	2.44	2.61	2.68	2.75	2.87	3.02	1.144	1.275	110.62	1.306	7819.31	2850.13	25669.32

Data Recap – Shifting perceptions on trade policy (Turkey tariffs, trade negotiations with China) continued to drive the stock market on a day-to-day basis. The economic data were largely inconsequential.

Retail Sales rose 0.5% in the advance estimate for July (+6.4% y/y), but June figures were revised lower. Ex-autos, sales rose 0.6% (+7.2% y/y). Contrary to expectations, vehicle sales rose 0.2% (despite a decline in unit sales, reported earlier) and gasoline sales rose 0.8% (despite a 0.6% decline in gasoline prices). Ex-autos, building materials, and gasoline, sales rose 0.6% (+5.7% y/y).

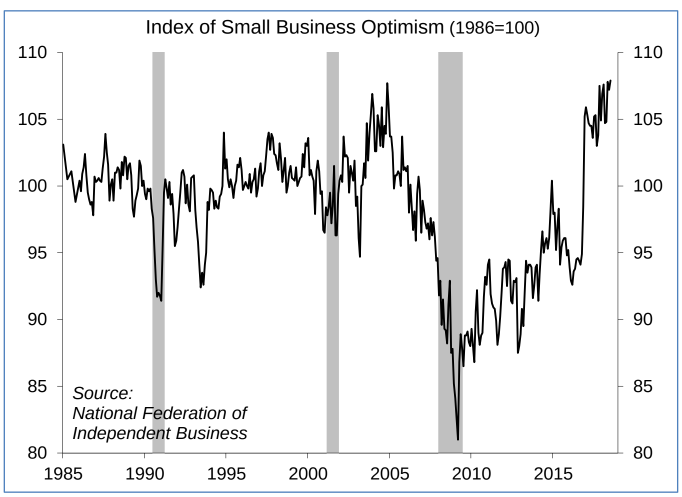


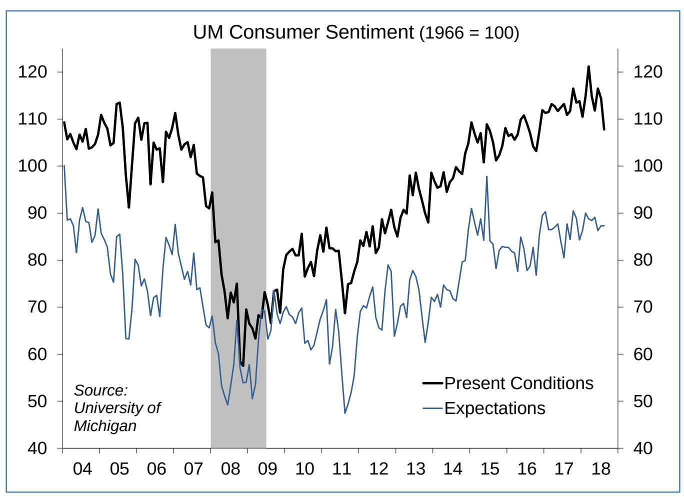


Industrial Production edged up 0.1% in July (+4.2% y/y), while figures for May and June were revised higher. Manufacturing output rose 0.3% (+3.0% y/y), up 0.2% ex-autos (+2.4% y/y).

Building Permits rose 1.5% in July, to a 1.311 million seasonally adjusted annual rate (+4.2% y/y). Single-family permits, the key figure in the report, rose 1.9% (+6.4% y/y). Unadjusted single-family permits for May-July were up 6.3% y/y (+4.4% in the Northeast, +2.9% in the Midwest, +5.5% in the South, and +10.6% in the West). **Housing Starts** rose 0.9%, to a 1.168 million pace (-1.4% y/y).

The Index of **Small Business Optimism** was little changed at 107.9 in July, vs. 107.2 in June and 107.8 in May. The general business outlook remained strong. Sales expectations improved. Hiring plans were robust. Capital spending plans were not much different than the trend over the last few years (although at the upper end of the range).





UM **Consumer Sentiment** fell to 95.3 in the mid-August assessment (the lowest since September), vs. 97.9 in July. Weakness was concentrated in evaluations of current conditions, which was reported to be related to pricing issues (that is, consumers appear to have become more sensitive to price increases even as overall inflation remains relatively low). Expectations, which are thought to be a driver of big-ticket purchases, held steady. However, buying perceptions for autos and homes continued to fall.

This Week – Powell's Fed Camp speech is expected to be the highlight, but it's unclear whether he will provide any clues on the expected course of monetary policy (the federal funds futures market is still placing a strong likelihood, about 96%, of a September 26 rate hike, and better-than-even odds, about 66%, of a December 19 follow-up). Home sales figures are not particularly market-moving (new home sales figures are erratic and existing home sales have been restrained by supply issues). The report on durable goods orders may be interesting, but there's often a lot of noise in the July figures.

Durable Goods Orders are expected to have risen moderately in July. Boeing reported a huge increase in orders in June (which fell back in July), but the June increase did not show up fully in the government data. There may be some catch-up. Ex-transportation, the trend has been moderate, but seasonal adjustment is tricky in July and figures may be distorted (±3.0%).

Fed Chair Jay Powell will speak at the Kansas City Fed's annual monetary policy symposium in Jackson Hole on Friday. In past years, this has often been a big deal for the financial markets. The theme this year is "Changing Market Structure and Implications for Monetary Policy." Powell's speech is titled *"Monetary Policy in a Changing Economy,"* which offers the possibility of a change in the Fed's current approach. While the focus is on Powell's speech, the more interesting debates (the impact of trade policy disruptions, the natural rate of unemployment) will occur in discussions in the hallways and around the grounds.

This Week:					***forecast***	last	last –1	comments
Monday	8/20		no significant data					
Tuesday	8/21		no significant data					
Wednesday	8/22	10:00	Existing Home Sales, mln	Jul	***5.40***	5.38	5.41	trend likely steadying
			% change		***+0.4***	-0.6	-0.7	supply constraints continue
		2:00	**FOMC Minutes**	8/01				some insight into the FOMC's thinking
Thursday	8/23	8:30	Jobless Claims, th.	8/18	***220***	212	214	a low trend
		10:00	New Home Sales, th.	Jul	***645***	631	666	volatile figures, but a moderate trend
			% change		***+2.2***	-5.3	+3.9	watch for revisions
		1:00	TIPS Auction					re-opened 5-year TIPS
Friday	8/24	8:30	**Durable Goods Orders**	Jul	***+0.4%***	+0.8%	-0.3%	where did Boeing's June orders go?
			ex-transportation		***+0.4%***	+0.2%	+0.3%	moderate, not especially strong
			nondef cap gds ex-aircraft		***+0.3%***	+0.2%	+0.7%	a lackluster trend
		10:00	**Powell Speaks**					at Jackson Hole conference
Next Week:								
Monday	8/27		Treasury Note Auction					2-year notes
Tuesday	8/28	8:30	Advance Econ Indicators	Jul				early look at 3Q18 GDP components
			merch. trade balance, $bln		***NF***	-67.9	-64.7	likely wider in early 3Q18
			wholesale inventories		***NF***	+0.1%	+0.3%	pace is expected to pick up in 3Q18
			retail inventories		***NF***	+0.1%	+0.4%	should be higher
		10:00	**CB Consumer Confidence**	Aug	***126.8***	127.4	127.1	still very high
		1:00	Treasury Note Auction					5-year notes
Wednesday	8/29	8:30	**Real GDP (2nd estimate)**	2Q18	***+4.0%***	+2.2%	+2.3%	+4.1% in the advance estimate
			Priv Dom Final Purchases		***+4.2%***	+2.0%	+4.4%	+4.3% in the advance estimate
		10:00	Pending Home Sales Index	Jul	***+0.4%***	+0.9%	-0.5%	choppy, but expecting a moderate trend
		11:30	FRN Auction					2-year FRNs
		1:00	Treasury Note Auction					7-year notes
Thursday	8/30	8:30	Jobless Claims, th.	8/25	***218***	***220***	212	a low trend
		8:30	Personal Income	Jul	***+0.3%***	+0.4%	+0.4%	wage growth soft in employment report
			Personal Spending		***+0.4%***	+0.4%	+0.5%	a moderate trend
			PCE Price Index ex-f&e		***+0.2%***	+0.1%	+0.2%	the core CPI rose 0.243%
			year-over-year		***+2.0%***	+1.9%	+1.9%	at the Fed's target
Friday	8/31	9:45	Chicago Business Barometer	Aug	***63.0***	65.5	64.1	likely to moderate somewhat
		10:00	UM Consumer Sentiment	Aug	***95.8***	97.9	98.2	95.3 at mid-month

Coming Events and Data Releases

September 3	Labor Day (markets closed)
September 4	ISM Manufacturing Index (August)
September 7	Employment Report (August)
September 26	FOMC Policy Decision, press conf.
November 6	Election Day
November 8	FOMC Policy Decision (no press conf.)
December 19	FOMC Policy Decision, press conf.
January 30	FOMC Policy Decision, press conf.
March 20	FOMC Policy Decision, press conf.