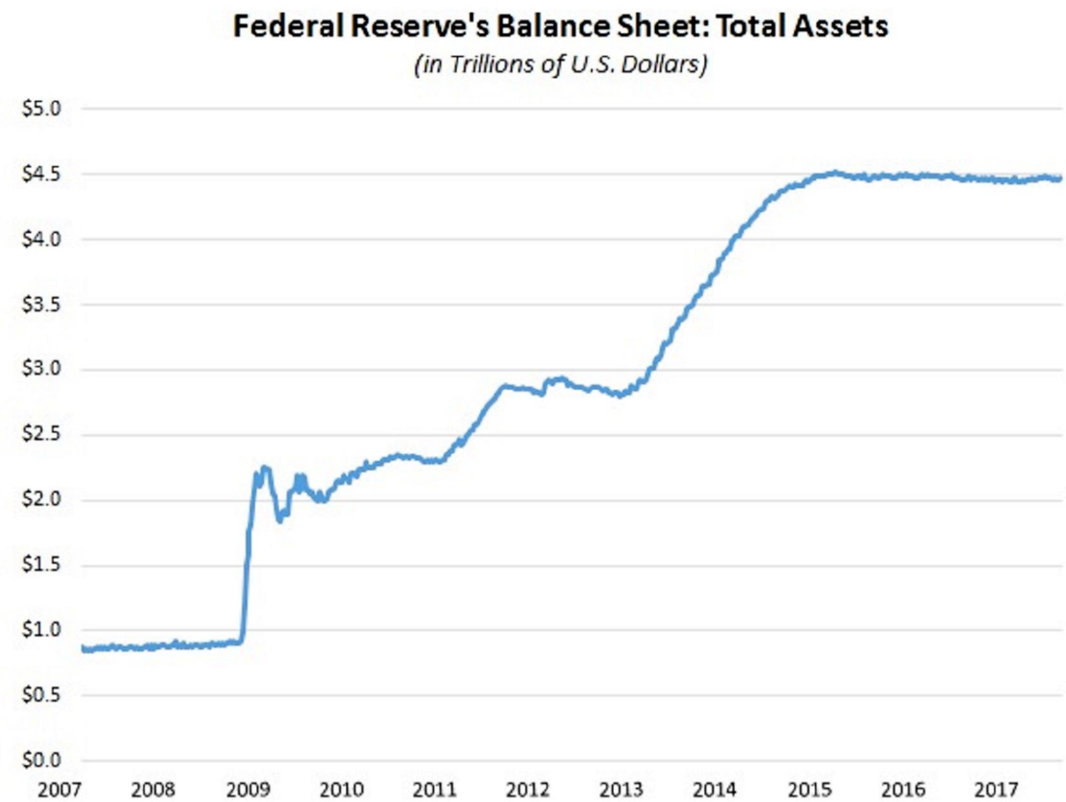

As expected, the Federal Open Market Committee (FOMC) voted to raise short-term interest rates at the conclusion of its June 13-14 meeting for only the third time since the financial crisis. After hiking the federal funds rate in December and March, the Federal Reserve increased rates by another 25 basis points, with a new target range of 1 to 1.25 percent. In making this decision, participants noted recent strengthening in the overall macroeconomy, including better data for consumer spending, business investment and hiring. Beyond this latest action, it is widely anticipated that the FOMC will increase rates one more time in 2017, perhaps as soon as its September 19-20 meeting. Participants also provided an update to the Federal Reserve's economic projections. The outlook improved marginally from what was released in March. Members now see the U.S. economy expanding 2.2 percent in 2017, up slightly from 2.1 percent three months ago. It forecasts 2.1 percent real GDP growth in 2018.

In addition to raising short-term rates, the FOMC also seeks to normalize the size of its balance sheet, which has ballooned to well over $4 trillion. Prior to the Great Recession, it never exceeded $1 trillion. The Federal Reserve set new policy guidelines for reducing its balance sheet, as outlined in an addendum that the committee passed unanimously. Starting later this year, the Federal Reserve will allow $10 billion per month in Treasury securities, agency debt and mortgage-backed securities to not be reinvested. It would then increase that amount by $10 billion each quarter until it reaches $50 billion per month. In doing so, the FOMC's actions would likely put further upward pressure on interest rates. Hence, its moves will be gradual in nature.

The inflationary picture has been positive for the Federal Reserve. While we had seen accelerations in both consumer and producer prices over much of the past few months, costs appear to have started to slow more recently. The consumer price index increased 1.9 percent year-over-year in May, its first reading below 2 percent since November, and producer prices for final demand goods and services have increased 2.4 percent since May 2016, easing a bit from April's 2.5 percent year-over-year pace, which was the fastest pace since February 2012. In terms of core inflation, which excludes food and energy costs, consumer prices have risen 1.7 percent over the past 12 months, with producer prices up 2.1 percent year-over-year. Both represent some deceleration from earlier in the year. For manufacturers, many of whom had been concerned about the pickup in pricing pressures in recent months, this should be a welcome development.

Despite the optimism in the Federal Reserve's moves, many of the economic data points released last week were disappointing. For instance, manufacturing production fell for the second time in the past three months, down 0.4 percent in May. Motor vehicles and parts production led the decline in May, down 2.0 percent for the month and off 1.5 percent year to date, as automotive demand has continued to be weaker than desired so far in 2017. Despite the easing in this latest release and some lingering challenges, the underlying data remain consistent with a manufacturing sector that has turned a corner and has moved in the right direction, especially relative to where it stood at this point last year. Manufacturing production has risen 1.4 percent over the past 12 months, expanding for the seventh consecutive month. In addition, manufacturers in the New York and Philadelphia Federal Reserve Bank surveys continued to be upbeat in their outlook, with activity strengthening in both June reports.

Consumer confidence was also weaker. The Index of Consumer Sentiment from the University of Michigan and Thomson Reuters declined in June to its lowest point since November, according to preliminary data. Political uncertainties played into this waning in assessments, with continuing wide disparities in opinions based on partisan affiliation. Along those lines, retail sales fell 0.3 percent in May, signaling a more cautious consumer than we would expect or prefer. Retail spending has increased 3.8 percent since May 2016, a modest pace that reflects some progress from what was seen at this point last year. Yet, the year-over-year growth rate was 5.6 percent in January, its fastest rate since March 2012, but it has eased since then.

Similarly, the housing market has also been softer than desired of late. New housing starts weakened again in May, dropping for the third straight month. Since reaching 1,288,000 units in February, housing starts have pulled back considerably. In May, single-family and multifamily starts slipped for the month, both eight-month lows. On a year-over-year basis, housing starts decreased 2.4 percent from May 2016's pace of 1,119,000. Yet, that mainly reflects a huge drop in multifamily activity, down 23.0 percent. In contrast, single-family starts have risen 8.5 percent, suggesting a better longer-term trend than the headline figures might seem to indicate. Along those lines, perhaps we will see a rebound during the summer. Homebuilder optimism remains strong, with respondents to that survey predicting healthy gains in activity over the next six months. I am also predicting a bounce-back, which is for 1.25 million starts by year's end.

There will only be a handful of economic releases out this week, with data focusing mainly on manufacturing and housing. IHS Markit will release new surveys on U.S. and Eurozone manufacturing activity for June, with Europe building on May's 73-month high in confidence as its economy continues to trend mostly in the right direction. Other highlights this week include the latest figures for existing and new home sales, the Kansas City Federal Reserve Bank's monthly survey and leading economic indicators.

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Economic Indicators

Last Week's Indicators:
(Summaries Appear Below)

Monday, June 12
None

Tuesday, June 13
NFIB Small Business Survey
Producer Price Index

Wednesday, June 14
Consumer Price Index
FOMC Monetary Policy Statement
Retail Sales

Thursday, June 15
Industrial Production
NAHB Housing Market Index
New York Fed Manufacturing Survey
Philadelphia Fed Manufacturing Survey

Friday, June 16
State Employment Report
University of Michigan Consumer Sentiment

This Week's Indicators:

Monday, June 19
None

Tuesday, June 20
None

Wednesday, June 21
Existing Home Sales

Thursday, June 22
Conference Board Leading Indicators
Kansas City Fed Manufacturing Survey

Friday, June 23
Markit Flash Manufacturing PMIs for the United States and Eurozone
New Home Sales

Summaries for Last Week`s Economic Indicators

Consumer Price Index

The Bureau of Labor Statistics reported that consumer prices edged down 0.1 percent in May, falling for the second time in the past three months. The lower figure mainly stemmed from reduced energy costs, down 2.7 percent, with gasoline prices off 6.4 percent. In contrast, food prices increased 0.2 percent for the second consecutive month. Over the past 12 months, food and energy costs have increased 0.9 percent and 5.4 percent, respectively. Overall, the consumer price index increased 1.9 percent year-over-year in May, its first reading below 2 percent since November. This suggests that the acceleration in pricing pressures that peaked at a 2.8 percent year-over-year rate in February has slowed since then. With that said, year-over-year consumer inflation was 1.0 percent in May 2016, suggesting that overall prices have still trended higher over the longer term.

Core consumer prices, which exclude food and energy costs, edged up 0.1 percent in May, mirroring its increase in April. Excluding food and energy costs, consumer prices have risen 1.7 percent over the past 12 months, pulling back from 2.0 percent in March and 1.9 percent in April. As such, overall pricing pressures remain modest and mostly under control for now.

FOMC Monetary Policy Statement

As expected, the Federal Open Market Committee (FOMC) voted to raise short-term interest rates at the conclusion of its June 13-14 meeting for only the third time since the financial crisis. After hiking the federal funds rate in December and March, the Federal Reserve increased rates by another 25 basis points, with a new target range of 1 to 1.25 percent. In making this decision, participants noted recent strengthening in the overall macroeconomy, including better data for consumer spending, business investment and hiring. Beyond this latest action, it is widely anticipated that the FOMC will increase rates one more time in 2017, perhaps as soon as its September 19-20 meeting. Such a decision, of course, would depend on continued improvements in economic activity, especially as the Federal Reserve remains "data dependent." At this meeting, there was one dissenter: Minneapolis Federal Reserve Bank President Neel Kashkari, who felt that incoming data did not warrant an increase just yet.

In addition to raising short-term rates, the FOMC also seeks to normalize the size of its balance sheet, which has ballooned to well over $4 trillion. Prior to the Great Recession, it never exceeded $1 trillion. The Federal Reserve set new policy guidelines for reducing its balance sheet, as outlined in an addendum that the committee passed unanimously. Starting later this year, the Federal Reserve will allow $10 billion per month in Treasury securities, agency debt and mortgage-backed securities to not be reinvested. It would then increase that amount by $10 billion each quarter until it reaches $50 billion per month. In doing so, the FOMC's actions would likely put further upward pressure on interest rates. Hence, its moves will be gradual in nature.

Meanwhile, participants also provided an update to the Federal Reserve's economic projections. The outlook improved marginally from what was released in March. Members now see the U.S. economy expanding 2.2 percent in 2017, up slightly from 2.1 percent three months ago. It forecasts 2.1 percent real GDP growth in 2018. In addition, the Federal Reserve predicts the unemployment rate falling to 4.3 percent in 2017 and 4.2 percent in 2018. In March, that figure was 4.5 percent for both years. The Federal Reserve foresees 1.7 percent core inflation in 2017, down from 1.9 percent in the prior projection. In terms of the federal funds rate, the FOMC median figures are consistent with three additional rate hikes in both 2018 and 2019.

Housing Starts and Permits

The Census Bureau and the Department of Housing and Urban Development reported that new housing starts weakened again in May, dropping for the third straight month. New residential construction fell from an annualized 1,156,000 in April to 1,092,000 in May, its lowest level since September. Since reaching 1,288,000 units in February, housing starts have pulled back considerably. This report is disappointing, especially since it was expected to rise and exceed 1.2 million again. Perhaps we will see a rebound during the summer. Homebuilder optimism remains strong (see below), with respondents to that survey predicting healthy gains in activity over the next six months. I am also predicting a bounce-back, which is for 1.25 million starts by year's end.

Looking at the May data, single-family (down from 826,000 to 794,000) and multifamily (down from 330,000 to 298,000) starts slipped for the month, both eight-month lows. Starts were sharply lower in the Midwest and South, unchanged in the Northeast and marginally higher in the West. On a year-over-year basis, housing starts decreased 2.4 percent from May 2016's pace of 1,119,000. Yet, that mainly reflects a huge drop in multifamily activity, down 23.0 percent. Note that multifamily starts can often be quite volatile from month to month. In contrast, single-family starts have risen 8.5 percent, suggesting a better longer-term trend than the headline figures might seem to indicate.

Meanwhile, housing permits also declined, down from 1,228,000 to 1,168,000 in this release. This ended nine consecutive months with permits exceeding 1.2 million units, with May's pace a 13-month low. Much like the starts data described above, these results are disappointing, particularly since permits are a proxy of future activity. Single-family (down from 794,000 to 779,000) and multifamily (down from 434,000 to 389,000) permitting both fell for the month. Overall, new residential construction permits have declined 0.9 percent since May 2016, off from 1,178,000 units last year. Nonetheless, single-family permits increased 6.0 percent year-over-year, with multifamily activity down 12.2 percent.

Industrial Production

The Federal Reserve reported that manufacturing production fell for the second time in the past three months, down 0.4 percent in May. After rebounding strongly in April, up 1.1 percent, this latest figure is a bit of a disappointment, suggesting a softening of activity following recent progress. Motor vehicles and parts production led the decline in May, down 2.0 percent for the month and off 1.5 percent year to date, as automotive demand has continued to be weaker than desired so far in 2017. Despite the easing in this latest release and some lingering challenges, the underlying data remain consistent with a manufacturing sector that has turned a corner and has moved in the right direction, especially relative to where it stood at this point last year.

Manufacturing production has risen 1.4 percent over the past 12 months, down from 1.6 percent in the previous report. Yet, it was the seventh consecutive positive year-over-year reading for manufacturing output and definite progress from the 0.3 percent year-over-year decline in May 2016. Similarly, manufacturing capacity utilization declined from 75.8 percent in April to 75.5 percent in May. For comparison purposes, utilization in the sector was 75.0 percent one year ago.

Digging into the underlying data, nondurable goods production edged up 0.1 percent in May, but durable goods output fell 0.8 percent. Beyond automotive, the largest declines included miscellaneous durable goods (down 2.1 percent), textile and product mills (down 1.8 percent), electrical equipment and appliances (down 1.6 percent), wood products (down 1.4 percent), printing and support (down 1.2 percent), fabricated metal products (down 0.7 percent) and paper (down 0.7 percent), among other sectors. In contrast, higher production levels included chemicals (up 1.1 percent), apparel and leather (up 0.7 percent) and machinery (up 0.1 percent).

Meanwhile, total industrial production was flat in May, slowing from its fastest monthly gain in more than three years in April (up 1.1 percent). Manufacturing output was the main drag on industrial production growth for the month, with mining and utilities production up 1.6 percent and 0.4 percent, respectively. Over the past 12 months, industrial production has risen 2.2 percent, its best reading since January 2015. The year-over-year pace was also a definite improvement from the 1.7 percent year-over-year decline in May 2016. Mining and utilities production grew 8.3 percent and 0.1 percent year-over-year in this release. At the same time, capacity utilization decreased from 76.7 percent-a 20-month high-to 76.6 percent.

NAHB Housing Market Index

The National Association of Home Builders (NAHB) and Wells Fargo reported that the Housing Market Index continued to reflect strength despite dipping slightly in June. The index decreased from 69 in May to 67 in June. Overall, it remained quite elevated and not far from March's reading of 71, which was the highest level since June 2005. Index values greater than 50 indicate strong builder confidence, with readings of 60 or more indicating very strong expectations for activity. With that said, NAHB Chief Economist Robert Dietz added that builders are concerned about "an ongoing shortage of skilled labor and buildable lots," both of which are "impeding stronger growth in the single-family sector."

Nonetheless, homebuilders have healthy assessments about single-family home sales over the next six months. The index for expected sales dropped from 78 to 76-still a very healthy figure. In the June data, sentiment ticked higher in the Midwest but was lower in other parts of the country.

New York Fed Manufacturing Survey

The Empire State Manufacturing Survey reported that manufacturing activity bounced back in June after softening in May. The composite index of general business conditions rose from -1.0 in May-its first decline in nine months-to 19.8 in June, its fastest pace since September 2014. Healthy accelerations in new orders (up from -4.4 to 18.1), shipments (up from 10.6 to 22.3) and the average workweek (up from 7.5 to 8.5) buoyed the strong rebound. The percentage of respondents saying orders had increased in the month rose from 20.7 percent in May to 35.1 percent in June. At the same time, hiring slowed somewhat (down from 11.9 to 7.7), even as growth in employment remained modest. The labor market has generally improved, up in four of the past six months after contracting sharply in the 10 months prior to that.

Overall, manufacturers in the New York Federal Reserve Bank's district were very upbeat about the next six months. Indeed, the forward-looking composite index ticked up from 39.3 to 41.7, matching the reading in February. At least half of those completing the survey predict better new orders and shipments in the months ahead, with 29.2 percent forecasting higher capital expenditures. With that said, the labor market figures were expected to be weaker, including employment (down from 17.2 to 12.3) and the average workweek (down from 5.2 to -5.4). The good news was hiring should continue to grow modestly, with the expected hiring index positive for the 10th straight month. Meanwhile, pricing pressures continue to be highly elevated moving forward (down from 38.1 to 33.1), even with a slight deceleration in June's survey.

NFIB Small Business Survey

The National Federation of Independent Business reported that the Small Business Optimism Index was flat in May, remaining at 104.5 for the second consecutive month. Sentiment among small business owners has remained highly elevated across the past six months despite easing from January's 105.9 reading, which was a 12-year high. Over that six-month period, the headline index has averaged 105.1. For comparison purposes, the index was 93.8 one year ago, illustrating the sizable uptick in confidence among small business leaders since November. Along those lines, the percentage of respondents suggesting the next three months would be a "good time to expand" edged down from 24 percent to 23 percent, which was the average over the past six months. In May 2016, just 9 percent said the same thing.

The percentage expecting sales to increase over the next three months ticked higher in May, up from 20 percent to 22 percent. While this was lower than the 31 percent in December, which was the highest level since October 2005, it continued to be a strong reading. One year ago, it was 1 percent. Likewise, the net percentage planning to add workers in the next three months increased from 16 percent to 18 percent, a four-month high. That suggests more small businesses are planning to add to their workforce. For instance, 9 percent were planning to hire as recently as August.

On the investment front, 62 percent of small business owners in May said they had made a capital expenditure in the past six months, up from 59 percent in April but down from March's 64 percent response, which was the highest reading since December 2013. Similarly, the percentage planning to make a capital expenditure in the next three to six months inched up from 27 percent to 28 percent. Small firms appear to be stepping up their capital spending relative to just a few months ago, which is encouraging.

The top "single most important problem" was taxes (22 percent), highlighting the need for comprehensive business tax reform. The quality of labor (19 percent), government regulations and red tape (13 percent) and the cost and availability of insurance (11 percent) also topped the list.

Philadelphia Fed Manufacturing Survey

The Federal Reserve Bank of Philadelphia reported that manufacturing activity expanded strongly in June once again. The composite index of general business activity decreased from 38.8 in May to 27.6

in June. To illustrate this recent progress, the headline index has averaged 31.4 through the first half of 2017, peaking at 43.3 in February, which was the best reading since November 1983. For comparison purposes, the average in the second half of 2016 was 9.1. In fact, growth in new orders accelerated in June (up from 25.4 to 25.9), with nearly 45 percent of survey respondents saying demand had risen since May. At the same time, other measures softened a bit in this release, even as they continued to expand at decent rates, including shipments (down from 39.1 to 28.5), employment (down from 17.3 to 16.1) and the average employee workweek (down from 21.7 to 20.5).

Meanwhile, manufacturers in the Philadelphia region remained quite optimistic about the next six months despite the forward-looking composite index falling from 59.5 in March-a 31-month high-to 31.3 in June. In this release, 47.5 percent and 49.6 percent expect new orders and shipments to rise in the coming months, respectively, with at least one-third seeing better hiring and capital spending. In a series of special questions, more than 60 percent predict a stronger second quarter, and 54.4 percent foresee a further acceleration in the third quarter. Those are uplifting statistics for the sector. On the downside, business leaders also see pricing pressures remaining elevated, even with some deceleration from previous months.

Producer Price Index

The Bureau of Labor Statistics reported that producer prices for final demand goods and services were flat in May, pulling back from a 0.5 percent gain in April. For manufacturers, producer prices for final demand goods edged down 0.1 percent in May, only slightly offsetting April's 0.7 percent increase. Both food and energy costs decreased, down 0.2 percent and 3.0 percent, respectively. On a year-over-year basis, final demand food and energy costs have risen 1.0 percent and 0.8 percent, respectively. Excluding food and energy, producer prices for final demand goods increased 0.1 percent.

Overall, producer prices for final demand goods and services have increased 2.4 percent since May 2016, easing a bit from April's 2.5 percent year-over-year pace, which was the fastest pace since February 2012. That represents a notable acceleration in inflationary pressures after being unchanged in August, and yet, this latest figure suggests that the pickup has stabilized-at least for now. In a similar way, core producer prices, which exclude food, energy and trade services, have grown 2.1 percent over the past 12 months, the same rate as in April but up from 0.9 percent one year ago.

Retail Sales

The U.S. consumer appears to be more cautious than we would expect, with disappointing retail sales figures in May, according to the Census Bureau. Spending at retailers fell 0.3 percent in May, nearly reversing the 0.4 percent gain in April and well below consensus estimates. Americans had been more willing to open their pocketbooks, especially relative to the caution seen at the beginning of 2016. This culminated in 5.6 percent year-over-year growth in January, its fastest pace since March 2012, but the year-over-year rate has eased since then. Since May 2016, retail spending has increased 3.8 percent. To be fair, sales continue to rise modestly, and year-over-year growth has trended mostly higher, up from 2.3 percent at this point last year.

Looking at the May report, the data were mixed but mostly lower. Retail segments with the largest declines in monthly sales included electronics and appliance stores (down 2.8 percent), gasoline stations (down 2.4 percent), miscellaneous store retailers (down 1.3 percent), department stores (down 1.0 percent) and sporting goods and hobby stores (down 0.6 percent), among others. While non-store retailers (up 0.8 percent), furniture and home furnishings stores (up 0.4 percent), clothing and accessory stores (up 0.3 percent) and food and beverage stores (up 0.1 percent) saw increases in May, each experienced reduced sales compared to April. It is worth noting the contrast between non-store retailers and department stores in this report, as retailers continue to grapple with the structural shifts taking place between online and brick-and-mortar spending habits.

Since May 2016, the largest gains in retail spending included building material and garden supply stores (up 10.8 percent), non-store retailers (up 10.2 percent), gasoline stations (up 6.2 percent), furniture and home furnishings stores (up 4.4 percent), motor vehicle and parts dealers (up 3.7 percent) and miscellaneous store retailers (up 3.4 percent). The gain for gasoline stations stemmed mainly from higher prices. Meanwhile, sporting goods and hobby stores saw the largest decrease, with a year-over-year decline in sales of 4.7 percent.

State Employment Report

Iowa created the most net new manufacturing jobs in May, according to the Bureau of Labor Statistics, adding 2,300 workers in the month. North Carolina (up 1,900), Missouri (up 1,800), Texas (up 1,800) and Alabama (up 1,000) also topped the list of manufacturing employment gains in May. In addition, Texas saw the greatest job gains over the past 12 months, with manufacturing employment in the state up 19,100 since May 2016. Other states with the fastest manufacturing job growth year-over-year included Florida (up 10,600), Michigan (up 9,800), South Carolina (up 7,400), Alabama (up 7,000) and Wisconsin (up 7,000).

The national unemployment rate fell to 4.3 percent in May, a 10-year low. Colorado had the lowest unemployment rate in the country at 2.3 percent. A number of states were not far behind, including North Dakota (2.5 percent), Hawaii (2.7 percent), Nebraska (2.9 percent), New Hampshire (2.9 percent) and South Dakota (2.9 percent). In contrast, Alaska (6.7 percent), New Mexico (6.6 percent), the District of Columbia (6.0 percent) and Louisiana (5.7 percent) had the highest unemployment rates.

University of Michigan Consumer Sentiment

The University of Michigan and Thomson Reuters reported that consumer confidence declined in June to its lowest point since November, according to preliminary data. The Index of Consumer Sentiment declined from 97.1 in May to 94.5 in June. In the release, Surveys of Consumers Chief Economist Richard Curtin attributed much of this to political uncertainties surrounding former FBI Director James Comey's testimony. As noted in prior surveys, there continue to be wide disparities in opinions based on partisan affiliation.

In these early June estimates, consumers were less upbeat about both current (down from 111.7 to 109.6) and future (down from 87.7 to 84.7) economic conditions. Despite the easing in this month's data, consumer confidence figures are consistent with 2.3 percent growth in personal spending in 2017. Final data will be released on June 30.