VNB® INSTITUTIONAL RESEARCH

Financial Market Weekly

5 June 2017

Economic Commentary

The two-hundred thousand plus job growth seen in the first two months of the year has given way to a much slower, sporadic pace of hiring. On Friday, the Bureau of Labor Statistics reported that only 138 thousand jobs were created in May well below the market consensus which called for 185 thousand. Government was the largest drag subtracting 9 thousand from the headline figure, mostly stemming from the State and Local levels.

In addition to the weak headline figure, average hourly earnings continued to underwhelm. On a year over year basis, earnings were up only 2.5 percent in May. Historically, when the unemployment rate was at 4.3 percent earnings would rise closer to 4.0 to 4.5 percent.

Rates Commentary

As we have moved closer to the FOMC announcement slated for later this month, the yield on the 2-year Treasury has inched backed towards its year-to-date high. Trade in the 2-year has certainly been tied to expectations for the Fed rate hike. Alternatively, longer dated Treasuries have moved in the opposite direction, particularly, over the last several weeks as the economic data has disappointed. The flattening yield curve has taken the 2-10 spread to 88bps, its lowest since October 2016.

Outlook

Despite the data coming in weaker than expected and, largely, inconsistent with the Federal Reserve's dual mandate, the probability for an increase in the target range has risen week after week to stand at nearly 96 percent as of this morning. Compared to one month ago, the probability for a rate hike was approximately 78 percent and arguably, the data was much stronger.

There is a Federal Open Market Committee meeting beginning on the 13th of this month which concludes on June 14 with a press conference from Chair Yellen. In addition, the Committee will release their revised economic projections. Even with the disappointing economic growth in the first quarter (coming in near 1.0%), job growth slowing over the last few months (from 216k in January to 138k in May) and inflation moving quickly away from the FOMC's 2 percent target (currently core PCE is 1.5%), the Fed will likely take advantage of the opportunity to push through one more hike. Should the data continue to sour however, the June hike may be the last for the year.

Contacts

Evan P. Bliss
Finance & Economics
(973) 305-8800 ext: 4087
ebliss@valleynationalbank.com

Christopher Philips
Structured Products
(973) 305-8800 ext: 4172
cphilips@valleynationalbank.com

Interest Rate Swap

Rate Market (vs. 2 weeks ago)
2y Swap: 1.51% (-1 bp)
5y Swap: 1.80% (-6 bps)
7y Swap: 2.01% (-7 bps)
10y Swap: 2.10% (-8 bps)
30y Swap: 2.38% (-9 bps)

Swap Spreads

Maturity
2-Year: +23 bps
5-Year: +8 bps
10-Year: -5 bps
30-Year: -43 bps

Source: Bloomberg, FRED