

Financial Market Weekly

8 August 2017

Economic Commentary

On Tuesday last week, the Bureau of Economic Analysis reported a pick-up in total vehicle sales in the U.S. after nearly six straight months of deceleration. For all domestically sold vehicles, the pace of sales increased from 17.0 million to 17.1 million, on a seasonally adjusted annual basis. The bump higher in sales was attributed to light automobile sales while light and heavy truck sales continued to trend lower. Over the past five years, heavy trucks sales and construction spending have maintained a fairly tight relationship. Should the sales within this segment continue to decelerate, it does not bode well for future construction spending.

Rates Commentary

At the Fed's FOMC meeting in late July, the Committee refrained from additional rate hikes although it introduced the likelihood that it would begin to reduce its \$4.5 trillion balance sheet relatively soon. Despite these comments, yields have generally moved lower over recent weeks. We suspect markets are finally waking up to the reality of sustained softening headline and core inflation. As a result, markets are discounting the probability of the Fed's future moves. The yield on the 2-year Treasury is lower by 4 basis points, trading at 1.36 percent as of this morning compared to the level seen prior to the July FOMC statement. By comparison, over the same period, the 10-year Treasury is lower by 6 basis points to 2.27 percent.

Outlook

After a flurry of information out last week on the health of the economy, we will get somewhat of a reprieve; although, there are a few important reports to take note of this week. On Tuesday, the Bureau of Labor Statistics will release data on the number of open jobs for June after showing a sharp decline in May. On Wednesday, productivity for the second quarter of 2017 will be released and to round out the week on Friday, we will receive the first reading on consumer price inflation for July. Headline consumer price inflation on a year over year basis has decelerated for four consecutive months. A surprise to the upside could lead the Fed into hiking sooner than markets expect which would cause yields to rise from current levels. At this point however, markets have assigned a 1, 7 and 47 percent probability for a hike at the September, November and December meeting, respectively.

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Interest Rate Swap

Rate Market (vs. 2 weeks ago)

2y Swap: 1.61% (-1 bp)
5y Swap: 1.90% (-1 bp)
7y Swap: 2.02% (unch)
10y Swap: 2.23% (-1 bp)
30y Swap: 2.53% (-2 bps)

Source: Bloomberg, FRED