John T. Halterman, Keith D. Dumas, Jeremy Frazie, and Carl McClurg Present:

MONTHLY ECONOMIC UPDATE

June 2016

THE MONTH IN BRIEF

Investors did not exactly "sell in May and go away" – the S&P 500 gained 1.53% last month. Oil prices settled into a sweet spot of sorts; they were high enough to soothe analysts, but not so high as to portend gas price spikes for consumers. Fundamental indicators pointed to an economy leaving its first-quarter doldrums behind; the real estate market looked especially hot. Hiring moderated, but retail sales, personal spending, and inflation picked up. It was enough to stir questions about an interest rate hike, and certain Federal Reserve officials publicly entertained that possibility.[1]

DOMESTIC ECONOMIC HEALTH

The May economic data stream brought many signals of a healthier economy. April brought a 1.0% jump in consumer spending, the largest monthly advance since August 2009. In accordance with that development, retail sales surged 1.3% in April.[2,3]

Service sector growth appeared to pick up as well in the year's fourth month: the Institute for Supply Management's non-manufacturing purchasing manager index came in at 55.7, 1.2 points higher than its March reading. ISM's manufacturing PMI dipped 1.0 points in April, but still showed sector expansion with a 50.8 mark. Reports from the federal government showed American industrial output up 0.7% for April and hard goods orders accelerating 3.4%.[3,4]

The Consumer Price Index rose a notable 0.4% in April, in contrast to 0.1% in March; the annualized gain for the core CPI through April was 2.1%. The country's primary wholesale inflation gauge exhibited roughly the same trend – the Producer Price Index advanced 0.2% for April after a 0.1% March retreat.[3]

First-quarter economic growth was adjusted upward by the Bureau of Economic Analysis. Near the end of May, the BEA said the economy expanded 0.8% in Q1, better than its initial estimate of 0.5%.[3]

One consumer confidence survey showed improvement in May, but another did not. The Conference Board's monthly index dipped for a second straight month to its lowest reading since November – a mark of 92.6, 2.1 points lower than its April reading. The University of Michigan's consumer sentiment index, on the other hand, ended May at 94.7.[2,3]

Investors and economists analyzed the Department of Labor's new jobs report at length early in the month. American payrolls showed a gain of just 160,000 jobs in April; did that telegraph weakness in the labor market, or an economy reaching full employment? While opinions were divided, statistics showed unemployment unchanged at 5.0% with underemployment (measured by the U-6 rate) ticking down to 9.7%. Yearly wage growth was a bright spot, reaching 2.5% in April.[5]

As May ended, there was a real sense that the health of the economy had improved from the first quarter, and three Federal Reserve officials (Janet Yellen, John Williams, and Eric Rosengren) had made some hawkish remarks about the merits of raising interest rates. In a May 27 conversation at Harvard University, Yellen stated that "probably in the coming months such a move would be appropriate."[6]

GLOBAL ECONOMIC HEALTH

Would the United Kingdom vote to leave the European Union in June? A pair of *Guardian* polls found public opinion leaning 52%-48% in favor of a "Brexit." Prime Minister David Cameron and Chancellor of the Exchequer George Osborne were adamantly against the move. Cameron called it "the self-destruct option" for the U.K. economy while Osborne saw a "DIY recession" ahead if voters approved a split from the EU in a June 23 national referendum. While the idea has gained popularity among the electorate, the U.K. treasury has forecast 520,000 lost jobs and a 3.6% dent to 2018 GDP as potential consequences. In the worst-case scenario, the Treasury sees roughly a 6% hit to the U.K.'s GDP and a 10% drop in its home prices.[7,8]

Eurostat showed the euro area jobless rate at 10.2% for April, the lowest level of unemployment seen since August 2011 and down from 11.0% a year earlier. Annualized inflation for the euro area was still negative (-0.2%) in April.[9]

As May ended, data showed India retaining its rank as the world's fastest-growing large economy. Its GDP for the first quarter was 7.9%, following 7.6% growth in 2015. Official PMIs from China were mildly encouraging. The April manufacturing PMI came in at 50.1, counting as a second consecutive month of expansion; the non-manufacturing PMI declined from 53.8 to 53.5.[10,11]

WORLD MARKETS

Global stock performance was all over the map in May. Brazil's Bovespa had it hardest, dropping 10.09%; Russia's RTS index sank 4.92%. At the other end of the spectrum, India's Sensex rose 4.14% while Japan's Nikkei 225 gained 3.41%. Australia's ASX 200 picked up 2.41%; Germany's DAX, 2.23%.[1]

Other notable gains and losses: Taiwan Weighted, +1.88%; CAC 40, +1.73%; FTSE Eurofirst 300, +1.56%; Euro Stoxx 50, +1.15%; TSX Composite, +0.82%; IBEX 35, +0.09%; FTSE 100, -0.18%; KOSPI, -0.54%; IPC All-Share, -0.71%; Shanghai Composite, -0.75%; Hang Seng, -1.20%; FTSE MIB, -3.09%.[1,12]

While the MSCI World index managed an 0.23% May rise, the MSCI Emerging Markets index fell 3.90% for the month.[13]

COMMODITIES MARKETS

May brought another big gain for oil. WTI crude futures rose 6.33% for the month, settling at $48.89 on the NYMEX on May 31. Other energy futures posted advances as well: natural gas, 6.68%; heating oil, 7.71%; unleaded gas, 0.31%. Corn gained 3.58%; soybeans, 5.63%; sugar, 7.22%; coffee, 0.66%; and cotton, 0.39%; on the other hand, cocoa lost 6.15%, and wheat lost 2.71%.[14]

The key metals went firmly south. Gold slipped 6.05% for the month on the COMEX; silver, 10.55%. They, respectively, ended May at $1,215.40 and $16.02. Platinum lost 8.75% on the month; copper, 8.11%. The U.S. Dollar Index headed north, rising from its April 29 close of 93.08 to a May 31 settlement of 95.83.[14,15]

REAL ESTATE

Simply put, April was a terrific month for the housing sector. Resales increased by 1.7% according to the National Association of Realtors, taking the annualized sales pace higher still. New home buying improved 16.6% in April to its hottest pace in eight years. March's S&P/Case-Shiller 20-city composite home price index showed a 5.4% yearly advance, meaning home prices were rising more than twice as fast as inflation.[16,17]

Two barometers of present and future housing activity also looked good. The NAR's pending home sales index rose a healthy 5.1% for April to a peak unseen since February 2006. The Census Bureau announced a 6.6% gain for housing starts (but also a 3.6% retreat for building permits).[3,16]

Freddie Mac's April 28 and May 26 Primary Mortgage Market Surveys showed very little change in mortgage rates. The average interest rate on a 30-year FRM went from 3.66% to 3.64%. Average interest for the 15-year FRM stayed put at 2.89%, while the 5/1-year ARM grew a touch more expensive, with the average interest rate rising to 2.87% from 2.86%.[18]

LOOKING BACK...LOOKING FORWARD

May was a very good month for the broad stock market, and the Nasdaq set the pace among the major indices. The tech-heavy benchmark advanced 3.62% during the month to a May 31 close of 4,948.05. The Russell 2000 performed well, settling at 1,154.79 after a 2.00% rise. The S&P 500's 1.53% gain led to a May 31 settlement of 2,096.96. Lagging behind, the Dow only rose 0.08% for the month to 17,787.20. Fear was in check, as the CBOE VIX ended May 9.62% lower at 14.19.[1,22]

% CHANGE	Y-T-D	1-YR CHG	5-YR AVG	10-YR AVG
DJIA	+2.08	-1.40	+8.30	+5.93
NASDAQ	-1.19	-2.65	+14.90	+12.71
S&P 500	+2.59	-0.70	+11.18	+6.51
REAL YIELD	5/31 RATE	1 YR AGO	5 YRS AGO	10 YRS AGO
10 YR TIPS	0.30%	0.39%	0.80%	2.48%

Sources: investing.com, bigcharts.com, treasury.gov – 5/31/16[1,19,20,21]

Indices are unmanaged, do not incur fees or expenses, and cannot be invested into directly. These returns do not include dividends. 10-year TIPS real yield = projected return at maturity given expected inflation.

May turned out to be much better for stocks than many investors anticipated. Is it unreasonable to expect further gains in June, given the chance of the Fed raising rates and the United Kingdom voting its way out of the EU? The market may end up pricing that rate hike in if the May jobs report is especially strong and Fed officials deliver further hints that a move is just ahead. News of a "Brexit" might do far greater harm to global markets. Investors will also want to keep an eye on the European Central Bank's latest policy statement, due in the first week of June. In short, this may be a month offering the chance for appreciable upset as well as appreciable upside. In the best-case scenario, it surprises us as nicely as May did.

UPCOMING ECONOMIC RELEASES: Here is the roll call for the rest of June...April wholesale inventories (6/9), the initial June University of Michigan consumer sentiment index (6/10), May retail sales and April business inventories (6/14), a Federal Reserve interest rate decision, the May PPI and the Fed's report on May industrial production (6/15), the May CPI (6/16), May groundbreaking and building permits (6/17), May existing home sales (6/22), May new home sales (6/23), the University of Michigan's final June consumer sentiment index and May durable goods orders (6/24), the final federal government estimate of Q1 GDP, the April S&P/Case-Shiller home price index and the June consumer confidence index from the Conference Board (6/28), and May pending home sales, the May PCE inflation gauge and May consumer spending (6/29).

Citations.

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