

Job Growth, Help from our Friends and Benign Policy Keeps the Expansion Going

The U.S. economy remains on track for an ongoing moderate expansion through 2018. If that turns out to be the case, by the end of 2018, this will be the second-longest economic expansion in U.S. history, still a few months short of the record 120 months from March 1991 to March 2001.

The U.S. expansion will be sustained with help from several key sources. First, we expect U.S. households to continue to spend. Even though job growth will likely ease over the next year, it will still be enough to keep the unemployment rate very low. With low unemployment, wages are increasing. This remains a controversial topic. Evidence suggests that the headline measures of wage growth, that look lower than expected now, are being distorted by the churn in the workforce as baby boomers retire and are replaced at lower salaries by millennials. From the point of view of the younger workers, they are getting raises. Ease in finding jobs, rising wages and house prices; as well as a strong stock market, are all supportive of consumer confidence and ongoing consumer spending.

We look for a continuing synchronized global expansion through 2018 and a weaker dollar to support U.S. exports. Recent manufacturing sector indicators show healthy conditions, supported, in part, by improving international trade. Europe appears to be finding its stride after a fitful post-crisis period. BREXIT negotiations will remain contentious. The UK economy will suffer as London sees its share of the European financial sector workforce decline. Frankfurt, Dublin and other European cities will gain.

U.S. fiscal policy should still be a positive even though expectations are lower. Congress must pass a debt ceiling agreement within the next few weeks to keep the federal government operational this fall. Failure to pass even a continuing resolution would jeopardize the federal government's credit rating, and push interest rates up. After the debt ceiling is addressed all eyes will be on tax reform. Tax reform still has the potential to boost consumer spending and encourage business investment, but the calendar keeps slipping back. We may not see the final tax package until early 2018. Expectations for infrastructure legislation are also lower and that calendar has been pushed back well into 2018.

We expect that monetary policy will be a positive factor by not being negative. Monetary policy is tightening and there is some risk that the Federal Reserve could overtighten and tip the economy back into recession. We look for the Fed to announce on September 20 that balance sheet reduction will begin in early October. The gradual increase in the amount of maturing assets that the Fed will let roll off its balance sheet (and not reinvest) is expected to result in a minor tightening of monetary conditions, equivalent to less than a 25-basis point increase in the fed funds rate. The ongoing discussion among Federal Reserve officials about lower than expected inflation suggests a lower terminal point for the fed funds rate for this cycle. In our September interest rate forecast, we have lowered the terminal fed funds rate to 1.88 percent. If interest rates stay low, that will be a plus for the U.S. economy.

With our limited space here, we cannot begin to address the economic impact of Hurricane Harvey on the South Texas economy. From a national point of view, we expect Harvey to subtract modestly from GDP growth in the third quarter. The recovery and rebuilding effort will provide a slight boost the U.S. economy in late 2017 through 2018.

U.S. Economic Outlook, Summary

	1Q'17a	2Q'17a	3Q'17f	4Q'17f	1Q'18f	2Q'18f	3Q'18f	4Q'18f	2016a	2017f	2018f
Real GDP (<i>Percent Change Annualized</i>)	1.2	3.0	2.5	2.9	2.5	2.1	2.0	2.1	1.5	2.2	2.4
CPI (<i>Percent Change Year-over-Year</i>)	2.6	1.9	2.3	1.6	1.2	1.8	1.4	1.9	1.3	2.1	1.6
Payroll Jobs (<i>Average Monthly Diff., Ths.</i>)	181.8	161.4	170.3	161.0	160.8	154.7	143.7	142.1	194.3	168.6	150.3
Unemployment Rate (<i>Percent</i>)	4.7	4.4	4.4	4.4	4.3	4.3	4.2	4.2	4.9	4.4	4.2
Federal Funds Rate (<i>Effective</i>)	0.70	0.95	1.15	1.17	1.38	1.42	1.63	1.67	0.40	0.99	1.53
10-Yr. Treasury Rate	2.44	2.26	2.24	2.25	2.50	2.57	2.80	2.87	1.84	2.30	2.69

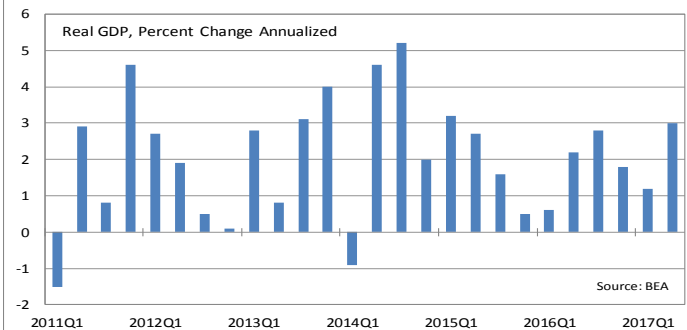
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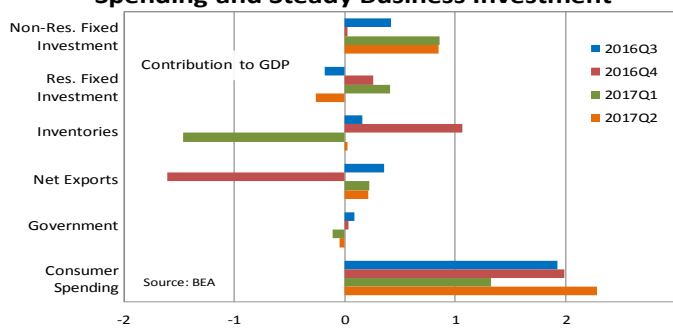
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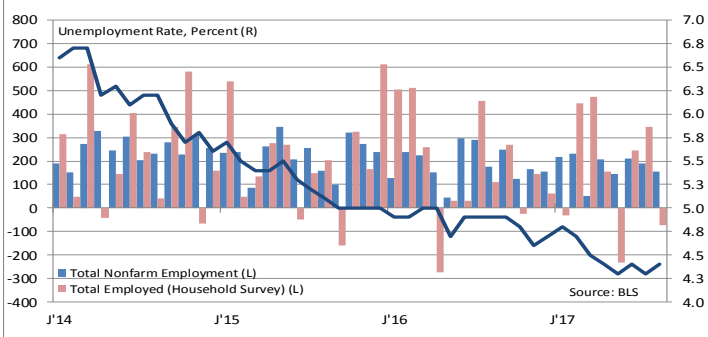
Q2 GDP Growth Revised Up to 3.0%



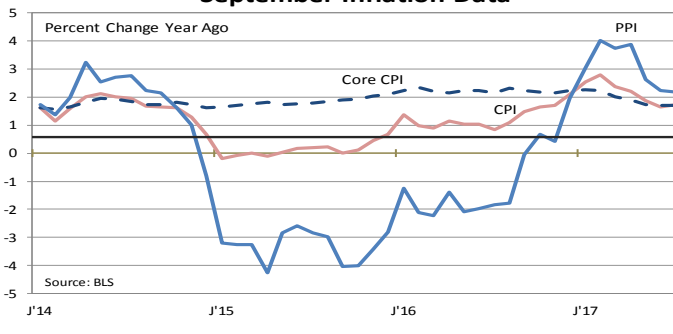
Q2 GDP Bolstered by Stronger Consumer Spending and Steady Business Investment



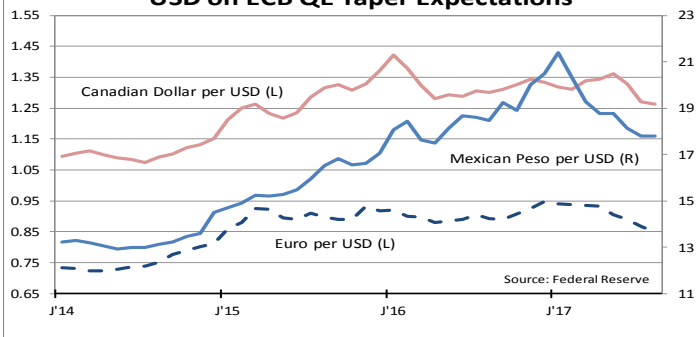
U.S. Added 156,000 Jobs in August



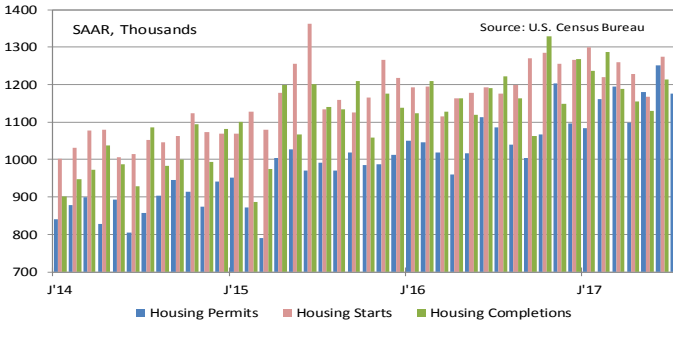
Recent Gas Price Gains will Appear in the September Inflation Data



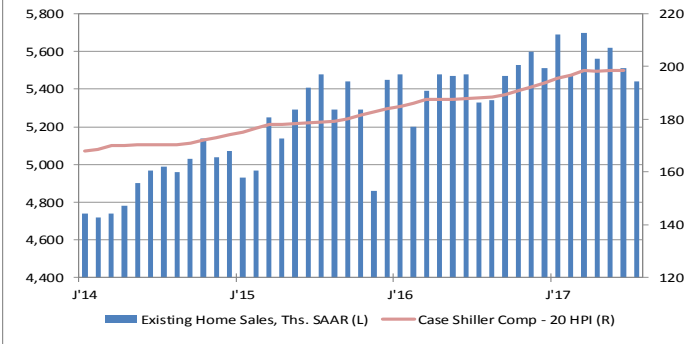
The Euro Saw a Summer Surge Against the USD on ECB QE Taper Expectations



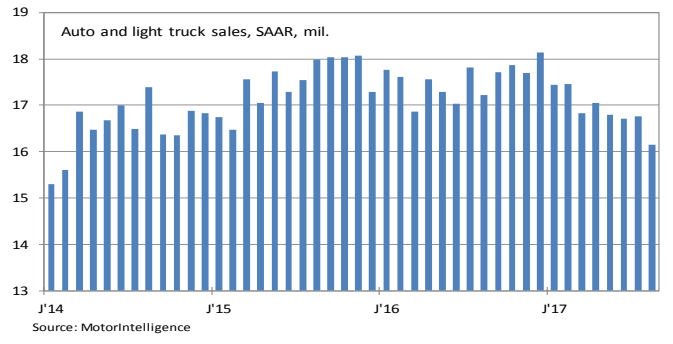
Housing Starts Remain Range Bound in 2017



Summer Slump for Existing Home Sales



August Auto Sales Dip to a 16.1 Million Rate



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	1Q'17a	2Q'17a	3Q'17f	4Q'17f	1Q'18f	2Q'18f	3Q'18f	4Q'18f	2016a	2017f	2018f
Output											
Nominal GDP (Billions \$)	19058	19247	19442	19643	19855	20030	20212	20407	18624	19347	20126
Percent Change Annualized	3.3	4.0	4.1	4.2	4.4	3.6	3.7	3.9	2.8	3.9	4.0
Real GDP (Chained 2009 Billions \$)	16903	17030	17133	17258	17363	17451	17538	17629	16716	17081	17495
Percent Change Annualized	1.2	3.0	2.5	2.9	2.5	2.1	2.0	2.1	1.5	2.2	2.4
Pers. Consumption Expenditures	11758	11854	11898	11970	12029	12084	12145	12202	11572	11870	12115
Percent Change Annualized	1.9	3.3	1.5	2.4	2.0	1.8	2.0	1.9	2.7	2.6	2.1
Nonresidential Fixed Investment	2264	2302	2330	2358	2384	2408	2433	2455	2210	2313	2420
Percent Change Annualized	7.1	6.9	5.0	4.9	4.5	4.2	4.1	3.6	-0.6	4.6	4.6
Residential Investment	606	595	596	595	595	596	598	601	587	598	598
Percent Change Annualized	11.1	-6.5	0.1	-0.2	0.1	0.3	1.5	2.3	5.5	1.8	-0.1
Change in Private Inventories	1	2	25	29	39	48	55	56	33	14	50
Net Exports	-622	-613	-613	-607	-613	-616	-627	-630	-586	-614	-622
Government Expenditures	2897	2894	2903	2917	2931	2935	2938	2949	2900	2903	2938
Percent Change Annualized	-0.6	-0.3	1.2	2.0	2.0	0.5	0.4	1.5	0.8	0.1	1.2
Industrial Prod. Index (2007=100)	103.7	105.0	105.2	105.8	106.2	106.5	106.7	107.0	103.1	104.9	106.6
Percent Change Annualized	1.6	5.2	0.6	2.2	1.5	1.2	1.0	0.8	-1.2	1.8	1.6
Capacity Utilization (Percent)	75.8	76.6	76.7	76.9	77.0	77.2	77.3	77.4	75.7	76.5	77.2
Prices											
CPI (1982-84=100)	244.1	243.9	246.0	246.1	247.0	248.2	249.5	250.8	240.0	245.0	248.9
Percent Change Annualized	3.1	-0.3	3.5	0.1	1.5	2.0	2.1	2.0	1.3	2.1	1.6
PCE Price Index (2009=100)	112.2	112.3	113.2	113.2	113.6	114.2	114.7	115.3	110.8	112.7	114.5
Percent Change Annualized	2.2	0.3	3.3	0.0	1.5	2.0	2.0	2.0	1.2	1.7	1.5
GDP Price Index (2009=100)	112.8	113.0	113.5	113.8	114.4	114.8	115.3	115.8	111.4	113.3	115.1
Percent Change Annualized	2.0	1.0	1.7	1.3	1.9	1.5	1.7	1.8	1.3	1.7	1.6
Producer Price Index, Finished Goods	196.8	197.0	198.3	198.1	198.9	199.9	201.0	202.0	191.9	197.6	200.5
Percent Change Annualized	6.3	0.3	2.6	-0.3	1.5	2.2	2.2	2.0	-1.0	3.0	1.5
Crude Oil, WTI (\$/barrel)	50.0	51.0	47.5	49.0	50.0	50.0	52.5	52.5	43.1	49.4	51.3
Labor Markets											
Payroll Jobs (Average Monthly Diff., Ths.)	181.8	161.4	170.3	161.0	160.8	154.7	143.7	142.1	194.3	168.6	150.3
Unemployment Rate (Percent)	4.7	4.4	4.4	4.4	4.3	4.3	4.2	4.2	4.9	4.4	4.2
Average Weekly Hours, Prod. Works.	33.6	33.7	33.7	33.7	33.7	33.6	33.6	33.6	33.6	33.7	33.6
Population (Millions)	325.1	325.8	326.4	327.1	327.7	328.4	329.0	329.7	323.5	326.1	328.7
Percent Change Annualized	0.8	0.8	0.8	0.8	0.8	0.8	0.8	0.8	0.7	0.8	0.8
Personal Income											
Average Hourly Earnings (\$)	21.86	22.00	22.14	22.28	22.43	22.59	22.75	22.92	21.56	22.07	22.67
Percent Change Annualized	2.0	2.5	2.6	2.6	2.8	2.8	3.0	2.9	2.5	2.4	2.7
Real Disp. Income (2009 Billions \$)	12680	12780	12810	12963	13091	13201	13305	13404	12608	12808	13250
Percent Change Annualized	2.9	3.2	0.9	4.9	4.0	3.4	3.2	3.0	1.4	1.6	3.4
Personal Saving Rate (Percent)	3.9	3.7	3.8	3.8	3.8	3.8	3.8	3.8	4.9	3.8	3.8
Housing											
Housing Starts (Ths., Ann. Rate)	1238	1165	1171	1155	1150	1147	1156	1164	1177	1182	1154
Ext. SF Home Sales (Ths., Ann Rate)	4993	4930	4903	4903	4902	4902	4905	4913	4828	4932	4906
New SF Home Sales (Ths., Ann Rate)	617	613	603	598	597	596	599	602	561	608	598
Case/Shiller HPI (Jan. 2000=100)	188.2	189.9	192.1	194.2	196.3	198.4	200.6	202.8	181.1	191.1	199.5
Year/Year Percent Change	5.6	5.7	5.8	4.9	4.3	4.5	4.4	4.4	5.1	5.5	4.4
Consumer											
Household Economic Stress Index	1.6	0.5	0.9	1.1	1.2	1.5	1.2	1.7	1.0	1.0	1.4
Auto Sales (Millions)	17.2	16.8	16.5	17.7	16.8	15.9	16.2	16.0	17.5	17.1	16.2
Interest Rates (percent per year)											
Federal Funds Rate (Effective)	0.70	0.95	1.15	1.17	1.38	1.42	1.63	1.67	0.40	0.99	1.53
Prime Rate	3.79	4.04	4.24	4.27	4.48	4.52	4.73	4.77	3.51	4.09	4.63
1-Month LIBOR	0.83	1.06	1.23	1.30	1.53	1.57	1.78	1.82	0.50	1.10	1.68
3-Month LIBOR	1.07	1.20	1.31	1.37	1.62	1.66	1.87	1.91	0.74	1.24	1.77
1-Yr. Treasury Rate	0.89	1.12	1.23	1.28	1.48	1.52	1.73	1.78	0.61	1.13	1.63
5-Yr. Treasury Rate	1.94	1.81	1.80	1.81	2.07	2.14	2.37	2.44	1.34	1.84	2.25
10-Yr. Treasury Rate	2.44	2.26	2.24	2.25	2.50	2.57	2.80	2.87	1.84	2.30	2.69
30-Year Fixed Rate Mortgage	4.17	3.99	3.86	3.88	4.15	4.23	4.47	4.55	3.65	3.98	4.35

a = actual f = forecast

September 5, 2017

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