

Baker Market Update: Week in Review

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So, what do you think Jerome Powell hears; “yanni” or “laurel”? More importantly, to whom will he listen; James Bullard or Loretta Mester? The reason that might be important is because Mr. Bullard, President of the St. Louis Fed, and Mrs. Mester, President of the Cleveland Fed, are both on the Federal Open Market Committee and, as such, will both have Chairman Powell’s ear when the FOMC meets next month. The thing is, Jim and Loretta are not on the same page. In fact, their outlooks are so disparate, Mr. Powell might wonder if these two central bankers are even looking at the same economy.

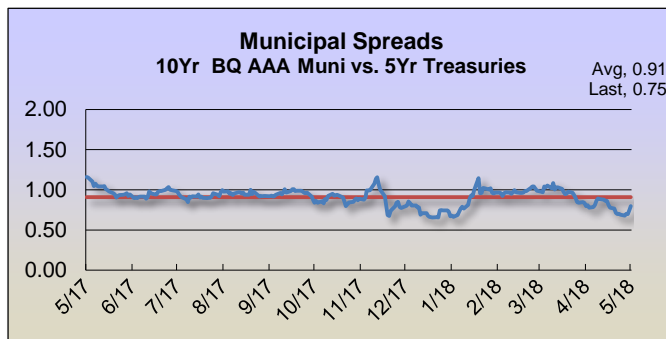
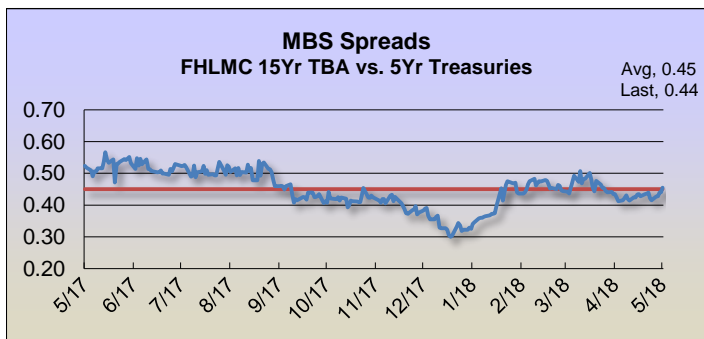
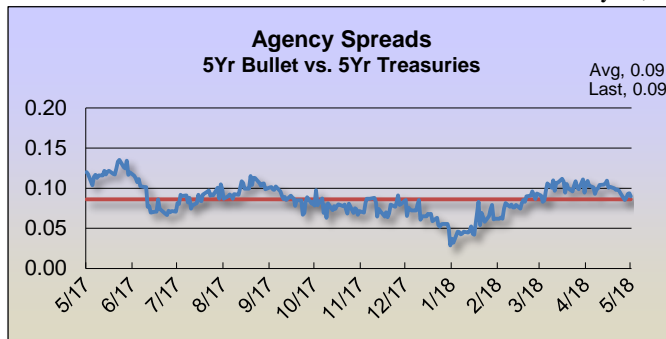
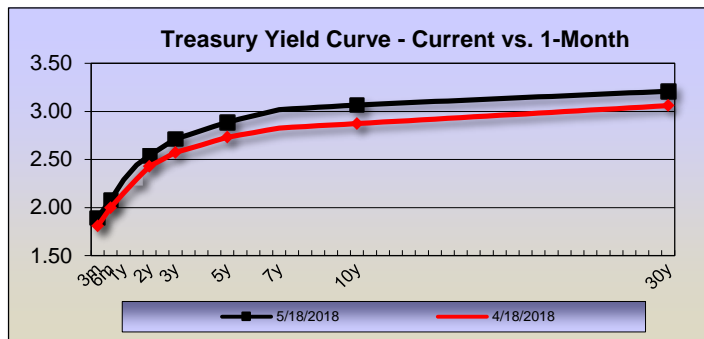
To make a long story less of one, Jim gave a speech to the Springfield, Missouri Chamber of Commerce this week and in that speech he shared his belief that the neutral rate for Fed Funds was reached when the committee last hiked rates in March. He believes *that* because he *doesn’t* believe that the Fed’s 2% goal for inflation has yet been achieved. He went on to say that his interpretation of market-based inflation expectations could keep that goal unattained for as long as five years. That’s not a typo; he said “five years.” And, that’s why he thinks the Fed should take a break from raising rates or, it runs the risk of inverting the yield curve. That is an outcome he thinks should be avoided. How can one not appreciate Jim’s love of understatement?

Mrs. Mester, on the other hand, was speaking this week in Paris when she said that a build-up of financial stability risks could best be avoided by the continuation of the Fed’s gradual removal of accommodation. Acknowledging that the inflation goal has yet to be achieved “in a sustained way”, she expects that it soon will be, and will, in turn, provide the justification for more rate hikes, possibly three more, in 2018. For her, the neutral rate is still quite a ways off. Could she not have just said that in Cleveland and saved on the airfare? Now, while both of these FOMC members have a seat, and a voice, at the big, shiny table, Jim doesn’t get to vote.

But, investors vote every day, and this week, they voted for inflation protection. The yield for Ten-Year Treasury Inflation Protected Securities (TIPS) hasn’t been this high since 2011. The non-TIPS Treasury market is also seeing higher rates with the Ten-Year now solidly above 3%. That condition was helped by an unexpectedly strong Empire Manufacturing report that showed that index of production vitality unexpectedly leaping to 20.1 from 15.8. Overall Industrial Production likewise saw a comeback from a first quarter dip with an April rise of 0.7%. But, Capacity Utilization at an unchanged 78% still describes a condition of significant output slack and makes one wonder why policy-makers continue to anticipate a huge tax-cut induced wave of capital expenditures. That anticipatory glow might dim a bit if they get wind of a recent report by Goldman Sachs that anticipates an additional \$650B worth of corporate stock buy-backs by year’s end. Apparently, there are a lot of corporate treasurers who didn’t get the memo about what they’re supposed to be doing with those tax savings.

And for the time being, consumers aren’t really following the script, either. Retail Sales notched a decent rise of 0.3% last month, but that was less than last month and right on top of expectations. Markets weren’t expecting a 3.7% drop in Housing Starts, but that’s what happened. Also happening was a 1.8% decline in Building Permits. And even if it’s *not* always sunny in Philadelphia, the sun was shining brightly on the Philadelphia Fed Business Outlook Survey Diffusion Index of General Conditions, or the PFBOSDIGC, for short. That measure experienced a monster jump to 34.4 from 23.2. That may not quite line up with other recent metrics, but, to the dismay of many, it’s not a linear world.

When the FOMC releases the minutes of its last meeting next week, maybe we’ll find out a little bit more about just what kind of world it is. And one small bit of advice for Mr. Powell; don’t believe everything you hear. Until next week, be careful out there.



Treasury Market -- Historical						Fixed Rate Market											
Maty	Current	1Wk Change	Historical			Maty /AL	N-Call Agency	US Swap	AAA BQ Muni		Tax Muni	Agency Calls - Euro					
			1 Mo	6 Mo	1 Yr				C-Corp ²	S-Corp ³		Mty	3Mo	6mo	1Yr	2Yr	
3mo	1.89	(0.01)	1.81	1.26	0.91	2yr	2.59	2.78	2.59	2.76	25.00	2Yr	1.94	1.94	1.94	-	
6mo	2.08	0.03	2.00	1.41	1.01	3yr	2.74	2.89	2.72	2.89	32.00	3Yr	2.10	2.11	2.11	2.10	
1yr	2.29	0.04	2.15	1.58	1.08	5yr	2.99	2.99	2.91	3.10	46.00	5Yr	2.19	2.22	2.24	2.24	
2yr	2.54	0.00	2.43	1.72	1.27	7yr	3.16	3.04	3.25	3.46	52.00	7Yr	2.42	2.47	2.52	2.53	
3yr	2.71	0.02	2.57	1.82	1.44	10yr	3.35	3.10	3.57	3.80	73.00	10Yr	2.57	2.62	2.69	2.72	
5yr	2.89	0.05	2.73	2.06	1.77	15yr	3.47	3.15	3.91	4.16	89.00	June TBA MBS					
7yr	3.02	0.08	2.83	2.23	2.04	20yr	3.60	3.16	4.14	4.41	77.00	Cpn	15Yr -Yld/AL		30Yr -Yld/AL		
10yr	3.07	0.10	2.87	2.34	2.23	25yr	3.72	3.15	4.22	4.49	79.00		2.00	3.32	5.1y		
30yr	3.21	0.10	3.06	2.78	2.90	30yr		3.13	4.30	4.57	81.00		2.50	3.22	5.3y		
													3.00	3.30	5.1y	3.57	9.9y
													3.50	3.21	2.9y	3.70	9.1y
												4.00			3.78	7.5y	
												4.50			3.79	6.4y	

* Interpolated

Key Market Indices					
Index	Current	1Wk Change	Historical		
			1 Mo	6 Mo	1 Yr
Fed Funds	1.75	--	1.75	1.25	1.00
Primary Discount	2.25	--	2.25	1.75	1.50
2ndary Discount	2.75	--	2.75	2.25	2.00
Prime Rate	4.75	--	4.75	4.25	4.00
Sec. O.N. Finance	1.74				
1 Month LIBOR	1.95	0.03	1.90	1.29	1.00
3 Month LIBOR	2.33	--	2.36	1.44	1.18
6 Month LIBOR	2.50	--	2.50	1.63	1.41
1 Year LIBOR	2.77	--	2.75	1.91	1.73
6 Month CD	2.45	--	2.49	1.59	1.46
1 Year CMT	2.32	0.05	2.16	1.60	1.08
REPO O/N	1.73	--	1.74	1.10	0.87
REPO 1Wk	1.78	--	1.77	1.20	0.95
CoF Federal	1.749	--	1.664	1.452	1.233
11th D. CoF (Mar)	0.814	--	0.816	0.729	0.583

FHLB Fixed Advance Rates					Fed Fund Futures	
Maturity	Chicago	Boston	Dallas	Topeka	Maturity	Rate
3mo	2.11	2.26	2.08	2.22	May-18	1.700
6mo	2.24	2.35	2.24	2.36	Jun-18	1.840
1yr	2.57	2.54	2.49	2.61	Jul-18	1.945
2yr	2.77	2.95	2.80	2.98	Aug-18	1.960
3yr	2.91	3.10	3.01	3.13	Sep-18	1.980
4yr	3.03	3.24	3.14	3.26	Oct-18	2.145
5yr	3.10	3.31	3.21	3.31	Nov-18	2.165
7yr	3.33	3.58	3.44	3.48	Dec-18	2.215
10yr	3.54	3.82	3.65	3.69	Jan-19	2.290
5yr Am	2.96		3.06	3.22	Feb-19	2.315
10yr Am	3.34		3.43	3.56	Mar-19	2.355

Weekly Economic Calendar						
This Week & Next						
Date	Release	Per.	Est.	Actual	Prior	Revised
05/15	Empire Manufacturing	May	15.00	20.10	15.80	--
05/15	Retail Sales Advance MoM	Apr	0.30%	0.30%	0.60%	0.80%
05/15	Retail Sales Ex Auto MoM	Apr	0.50%	0.30%	0.20%	0.40%
05/15	Retail Sales Ex Auto and Gas	Apr	0.40%	0.30%	0.30%	0.40%
05/15	Retail Sales Control Group	Apr	0.40%	0.40%	0.40%	0.50%
05/15	Business Inventories	Mar	0.10%	0.00%	0.60%	--
05/15	NAHB Housing Market Index	May	69.00	70.00	69.00	68.00
05/15	Total Net TIC Flows	Mar	--	-\$38.5b	\$44.7b	\$47.5b
05/15	Net Long-term TIC Flows	Mar	--	\$61.8b	\$49.0b	--
05/16	MBA Mortgage Applications	5/11	--	-2.70%	-0.40%	--
05/16	Housing Starts	Apr	1310k	1287k	1319k	1336k
05/16	Housing Starts MoM	Apr	-0.70%	-3.70%	1.90%	3.60%
05/16	Building Permits	Apr	1350k	1352k	1354k	1377k
05/16	Building Permits MoM	Apr	-2.10%	-1.80%	2.50%	4.10%
05/16	Industrial Production MoM	Apr	0.60%	0.70%	0.50%	0.70%
05/16	Manufacturing (SIC) Production	Apr	0.50%	0.50%	0.10%	0.00%
05/16	Capacity Utilization	Apr	78.40%	78.00%	78.00%	77.60%
05/16	Mortgage Delinquencies	1Q	--	4.63%	5.17%	--
05/16	MBA Mortgage Foreclosures	1Q	--	1.16%	1.19%	--
05/17	Initial Jobless Claims	5/12	215k	222k	211k	--
05/17	Continuing Claims	5/5	1780k	1707k	1790k	1794k
05/17	Philadelphia Fed Business Outlook	May	21.00	34.40	23.20	--
05/17	Bloomberg Economic Expectations	May	--	54.50	52.50	--
05/17	Bloomberg Consumer Comfort	5/13	--	54.60	55.80	--
05/17	Leading Index	Apr	0.40%	0.40%	0.30%	0.40%
05/21	Chicago Fed Nat Activity Index	Apr	--	--	10.00%	--
05/22	Richmond Fed Manuf. Index	May	8.00	--	-3.00	--
05/23	MBA Mortgage Applications	5/18	--	--	-2.70%	--
05/23	Markit US Manufacturing PMI	May P	56.50	--	56.50	--
05/23	Markit US Services PMI	May P	54.80	--	54.60	--
05/23	Markit US Composite PMI	May P	--	--	54.90	--
05/23	New Home Sales	Apr	678k	--	694k	--
05/23	New Home Sales MoM	Apr	-2.30%	--	4.00%	--
05/23	FOMC Meeting Minutes	5/2	--	--	--	--
05/24	Initial Jobless Claims	5/19	220k	--	222k	--
05/24	Continuing Claims	5/12	1750k	--	1707k	--
05/24	House Price Purchase Index QoQ	1Q	0.70%	--	1.60%	--
05/24	FHFA House Price Index MoM	Mar	--	--	0.60%	--
05/24	Bloomberg Consumer Comfort	5/20	--	--	54.60	--
05/24	Existing Home Sales	Apr	5.55m	--	5.60m	--
05/24	Kansas City Fed Manf. Activity	May	23.00	--	26.00	--
05/25	Durable Goods Orders	Apr P	-1.40%	--	2.60%	--
05/25	Durables Ex Transportation	Apr P	0.50%	--	0.10%	--
05/25	Cap Goods Orders Nondef Ex Air	Apr P	0.70%	--	-0.40%	--
05/25	Cap Goods Ship Nondef Ex Air	Apr P	0.40%	--	-0.80%	--
05/25	U. of Mich. Current Conditions	May F	--	--	113.30	--
05/25	U. of Mich. 1 Yr Inflation	May F	--	--	2.80%	--

MBS Prepayments ⁴						
3-Month CPR						
Type	2.0	2.5	3.0	3.5	4.0	4.5
FN 10y	11.7	12.6	14.0	16.1	24.6	30.2
FH/FN 15y	5.2	5.4	6.4	13.0	14.9	18.3
GN 15y	7.4	10.9	12.4	12.1	12.8	12.8
FH/FN 20y		5.6	7.1	8.4	10.2	12.5
FH/FN 30y	3.0	4.5	3.1	4.9	8.4	13.7
GN 30y	6.4	9.0	10.9	14.0	14.2	15.9
CPR Projections						
Type	2.0	2.5	3.0	3.5	4.0	4.5
FN 10y	11.7	11.2	12.0	17.2	19.4	21.9
FH/FN 15y	7.4	8.1	8.9	11.1	15.7	25.0
GN 15y	7.0	10.0	11.9	13.9	12.7	12.5
FH/FN 20y	3.1	6.6	7.7	9.4	11.5	13.7
FH/FN 30y	4.8	5.7	5.9	7.0	9.7	12.3
GN 30y	5.7	7.8	8.8	10.9	16.0	19.5

Other Markets					
Index	Current	1Wk Chng	Historical		
			1 Mo	6 Mo	1 Yr
Currencies					
Japanese Yen	110.75	1.36	107.23	112.62	111.49
Euro	1.18	(0.02)	1.24	1.17	1.11
Dollar Index	93.67	1.13	89.62	93.66	97.88
Major Stock Indices					
Dow Jones	24,721	(110)	24,748	23,358	20,663
S&P 500	2,715.5	(12.3)	2,708.6	2,578.9	2,365.7
NASDAQ	7,370.4	(33)	7,295.2	6,782.8	6,055.1
Commodities					
Gold	1,290.7	(30.0)	1,351.2	1,296.5	1,252.8
Crude Oil	71.39	0.69	68.47	56.55	49.35
Natural Gas	2.86	0.06	2.74	3.10	3.18
Wheat	514.3	24.8	475.3	427.3	425.8
Corn	403.3	13.5	383.0	343.0	366.0

Notes	
1 Call Agy = Maturity at left w/ a 1-Year Call at Par	
2 Muni TEY (21% Fed, 0.5% CoF)	
3 S-Corp TEY Muni (29.6%, no TEFERA)	
4 MBS Prepayments are provided by Bloomberg	

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