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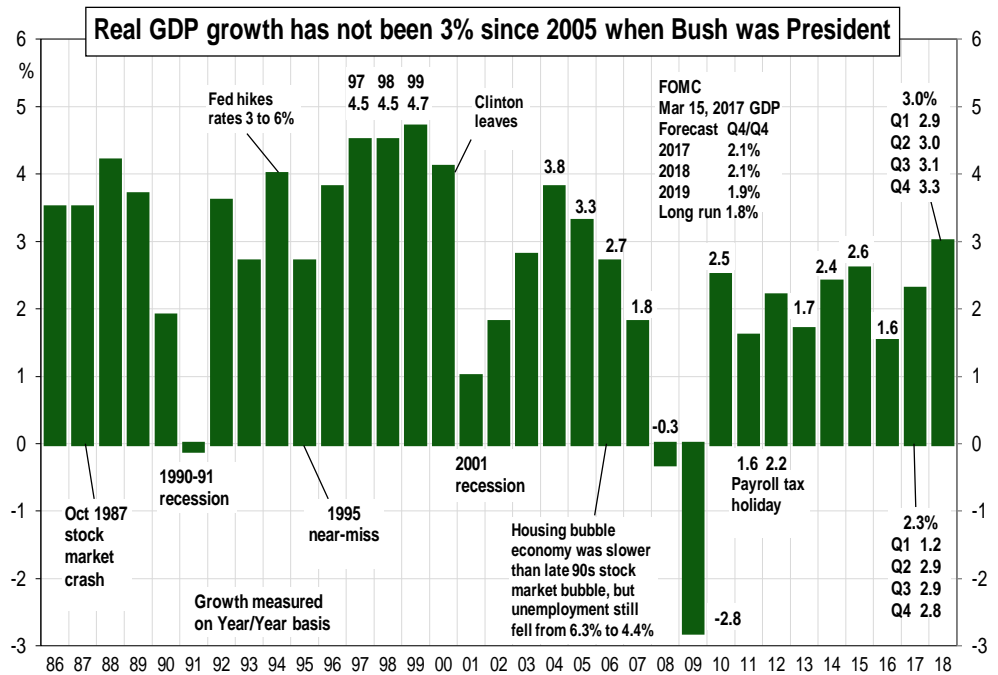
1.2% GDP NOW IN FIRST QUARTER BETTER THAN 0.7% BEFORE

Real GDP growth was revised up in the first quarter this week to 1.2% from the 0.7% estimate a month ago.

Why was growth half a percentage point higher? The reasons were mixed with some of the drag on spending made less so. Stronger spending revisions were seen in consumer expenditures on services, and business investment on “intellectual property,” which is software, R&D, and Entertainment. The stronger growth at the start of the year adds a tenth on our full year 2017 forecast to 2.3%. We are still thinking 3% in 2018, not ruling it out anyway, while the Fed forecasts in 2018 are for just 2.1% growth.

One of the new administration officials has said that the definition of Trump economics was 3% GDP. Growth of 3% is not that much higher than the trend in 2014-15, and a lot lower than the “double-GDP” campaign pledge

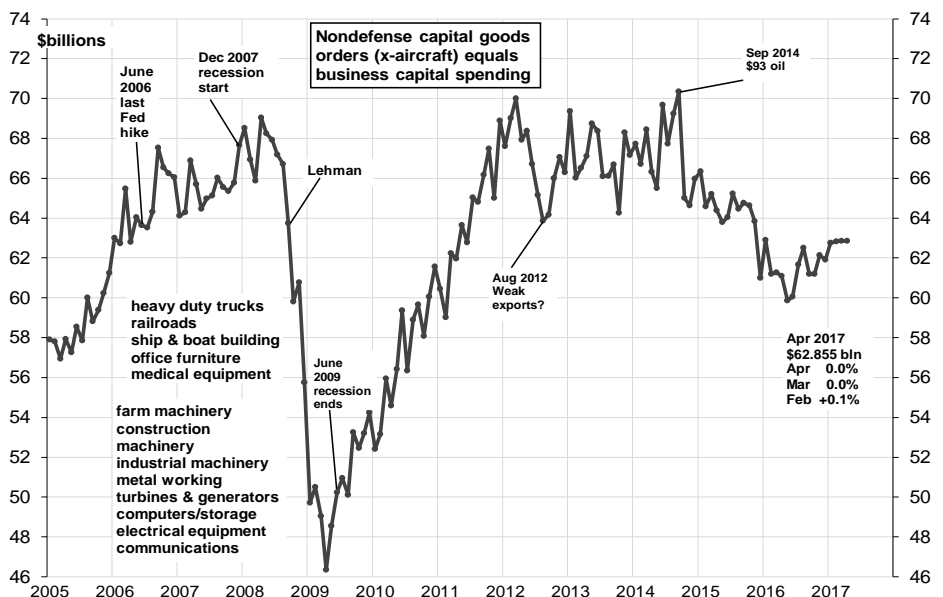
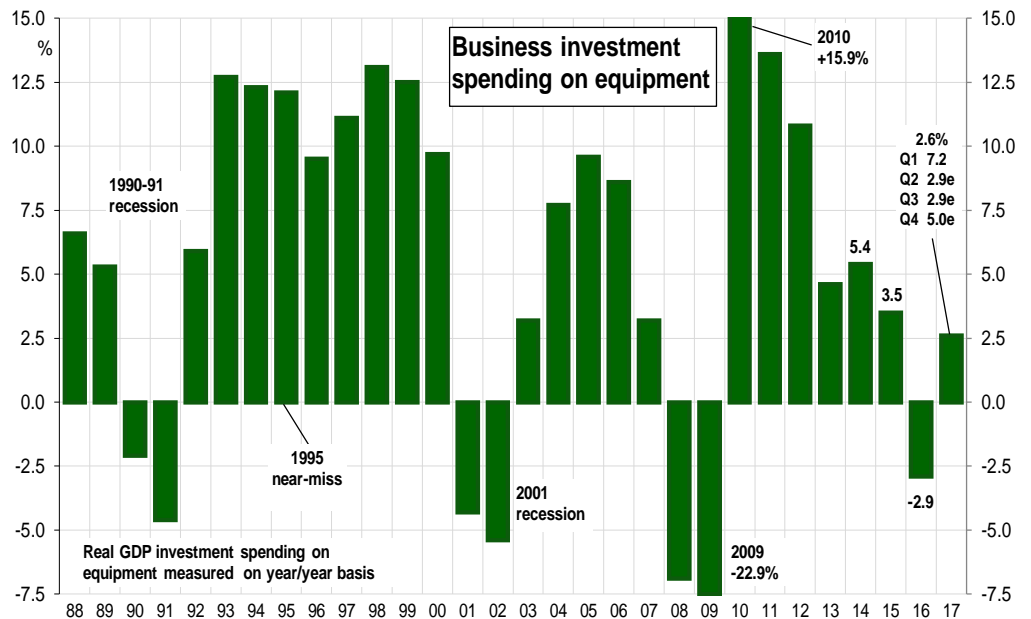
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	Q1 16	Q2 16	Q3 16	Q4 16	Q1 17p	Q1 17r
REAL GDP	0.8	1.4	3.5	2.1	0.7	1.2
REAL CONSUMPTION	1.6	4.3	3.0	3.5	0.3	0.6
CONSUMPTION	1.1	2.9	2.0	2.4	0.2	0.4
Durables	-0.1	0.7	0.8	0.8	-0.2	-0.1
Nondurables	0.3	0.8	-0.1	0.5	0.2	0.2
Services	0.9	1.4	1.3	1.1	0.2	0.4
INVESTMENT	-0.6	-1.3	0.5	1.5	0.7	0.8
Business Plant & Equipment and Intellectual Property	0.0	-0.1	0.3	-0.1	0.6	0.7
Homes	-0.6	-0.2	-0.3	0.1	0.5	0.4
Inventories	0.2	0.4	0.1	0.1	0.1	0.3
Exports	0.3	-0.3	-0.2	0.4	0.5	0.5
Imports	-0.4	-1.2	0.5	1.0	-0.9	-1.1
GOVERNMENT	-0.1	0.2	1.2	-0.6	0.7	0.7
Federal defense	0.1	0.0	-0.3	-1.3	-0.6	-0.6
Federal nondefense	0.3	-0.3	0.1	0.0	-0.3	-0.2
State and local	-0.1	-0.1	0.1	-0.1	-0.2	-0.2
Nondefense	0.0	0.1	0.1	0.1	0.0	0.0
State and local	0.4	-0.3	0.0	0.1	-0.2	-0.1

Below line: Percentage point contributions to Q1 17 1.2% real GDP
 Third estimate for Q1 is Thursday, June 29

that was more like 4% (double the “2% trend”) Growth was 2.6% in 2015, before slowing to 1.6% in 2016 on a temporary fall in inventories call it and the oil crash which dragged down business spending on structures and equipment. One reason for cutting corporate taxes is to boost business capex investment spending. The jury is out on whether investment will increase by giving corporations more after-tax income. It is not just the Trump economics team that wants more capex and growth. The Yellen-led Federal Reserve wants to see more business investment, and this is one reason they are keeping the cost of borrowing at these extraordinarily low levels.



Business spending is getting all the scrutiny right now. R&D dollars keep flowing for all the talk rising 9.6% at an annual rate in Q1 2017 after a 6.9% gain in 2016. Business equipment spending rebounded strongly in the first quarter, but nondefense capital goods orders ex-aircraft from Friday’s durable goods report show no movement in March and April. One of the tax reforms mentioned is the immediate expensing of equipment

purchases, so it is possible that some April durable goods purchases are being delayed. On the other hand, most of the durables weakness had

\$BLN Nominal GDP expenditures	Q4 15 YOY%	Q1 16	Q2 16	Q3 16	Q4 16 YOY%	Q1 17 Annual rate
Equipment & Intellectual Property	1823.5 4.4	1806.4	1817.4	1813.2	1822.9 0.0	1858.2 7.7%
EQUIPMENT	1092.6 4.2	1066.3	1058.7	1049.3	1053.5 -3.6	1074.3 7.9%
Information processing equipment	322.1 4.6	319.9	316.8	322.8	324.4 0.7	333.0 10.6%
Computers	75.4 -7.1	76.0	78.2	77.0	74.4 -1.3	77.5 16.7%
Other processing equipment 1	246.6 8.7	243.9	238.6	245.8	250.0 1.4	255.4 8.6%
Industrial equipment	224.7 3.8	222.2	227.3	226.1	228.7 1.8	233.8 8.9%
Transportation equipment	310.7 10.3	301.3	297.6	286.7	286.6 -7.8	292.6 8.4%
Other equipment 2	235.1 -3.2	222.9	217.0	213.7	213.8 -9.1	215.0 2.2%
INTELLECTUAL PROPERTY	730.9 4.9	740.1	758.7	763.9	769.4 5.3	783.9 7.5%
Software	330.1 3.8	336.0	339.4	342.6	343.7 4.1	348.4 5.5%
Research & Development (R&D)	320.3 5.7	323.0	337.9	338.8	342.3 6.9	350.5 9.6%
Entertainment, literary, artistic	80.6 6.2	81.1	81.4	82.5	83.4 3.5	85.0 7.7%

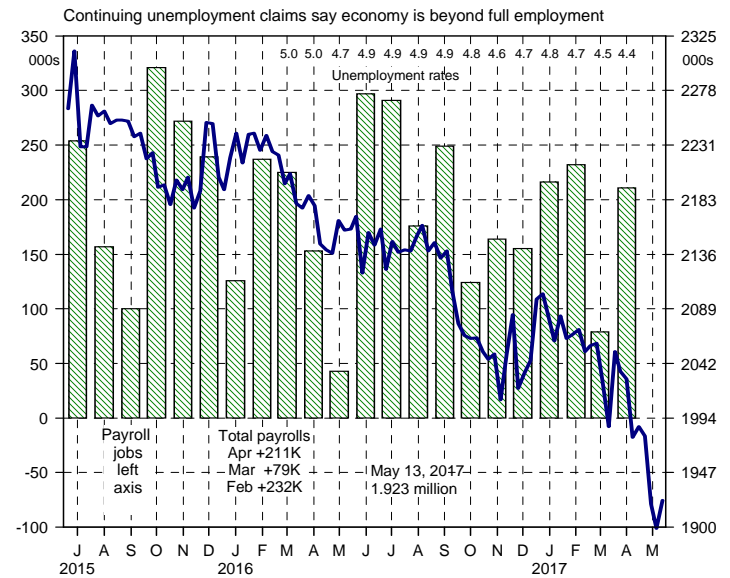
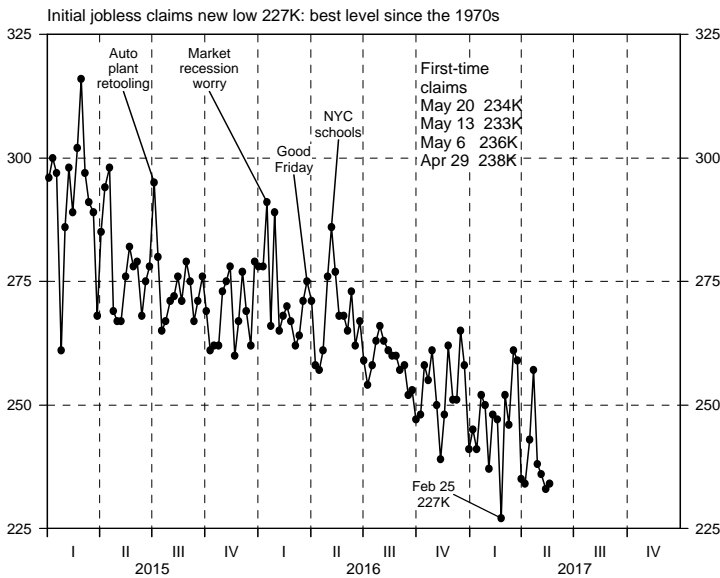
1 Communication, medical, photocopy, office and accounting equipment; nonmedical instruments
 2 Furniture; agriculture, construction, mining/oilfield, and service industry machinery; electrical equipment

been limited to farm machinery and oil & gas equipment orders. Too early to say whether Washington uncertainty is back on as a risk factor for the economy.

JOBLESS CLAIMS—BETTER THAN BEST TIMES NOW FOR LABOR MARKET

Unemployment claims were 234,000 in the May 20 week. There have now been four straight weeks that jobless claims have been down low in the 230,000 range. The labor market couldn't be any stronger according to jobless claims. It shows that businesses are wisely hoarding labor and not laying off workers because there are no skilled workers to fill these jobs at corporations and companies across the country. The Friday, June 2 monthly payroll jobs number could be another 200K-plus.

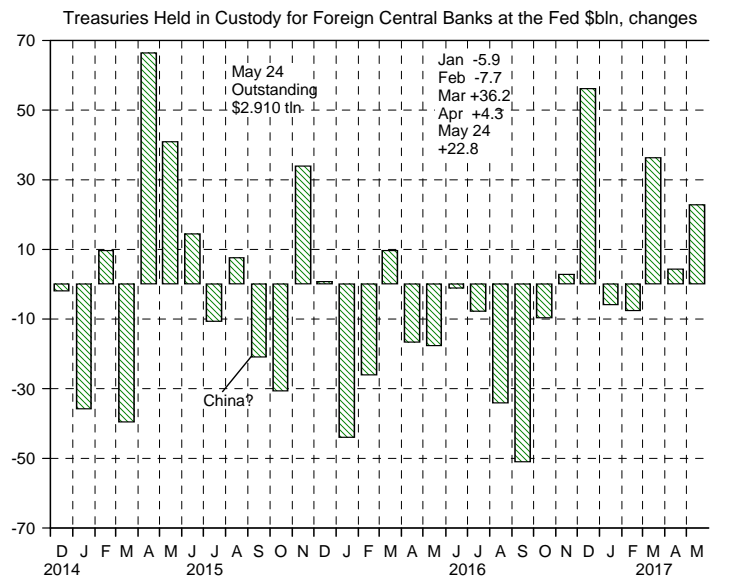
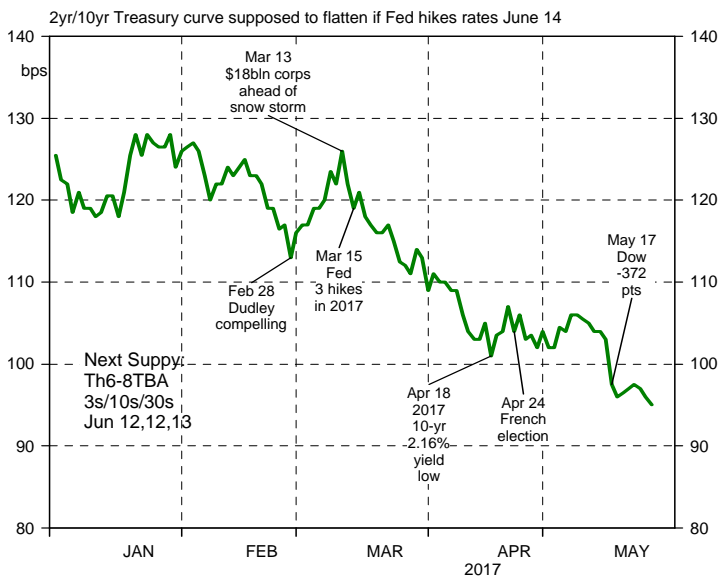
President takes Office	Unemployment
Clinton	Jan 1993 7.3%
Bush	Jan 2001 4.2%
Obama	Jan 2009 7.8%



TREASURY CURVE BREAKS 100 BPS, MORE NARROWING TO WAIT ON FED

The yield curve between 2-yrs and 10-yrs was 95 bps on Friday versus 96 bps last week. 10-yr yields had come down further from 2.40% in the prior week on the Trump Comey Russia revelations, in no particular order, falling with the Wednesday, May 17 Dow industrials steep 372 point drop, the biggest sell-off since the election. Stocks rallied back this week, the S&P 500 at least at record highs, but 10-yr yields stayed down in the dumps within a tight range of the closes from 2.25 to 2.28 percent.

	31-Mar 2017	Q2 2017	Q3 2017	Q4 2017	Q1 2018	Q2 2018	Q3 2018
30-Yr Bond	3.03	3.10	3.20	3.40	3.60	3.70	3.80
10-Yr Note	2.40	2.50	2.70	3.00	3.20	3.40	3.50
5-Yr Note	1.93	2.10	2.40	2.70	3.00	3.20	3.30
2-Yr Note	1.25	1.50	1.75	2.00	2.25	2.50	2.75
3-month Libor	1.15	1.50	1.70	1.95	2.20	2.45	2.70
Federal Fund Rate	1.00	1.25	1.50	1.75	2.00	2.25	2.50
2s/10s spread	115	100	95	100	95	90	75



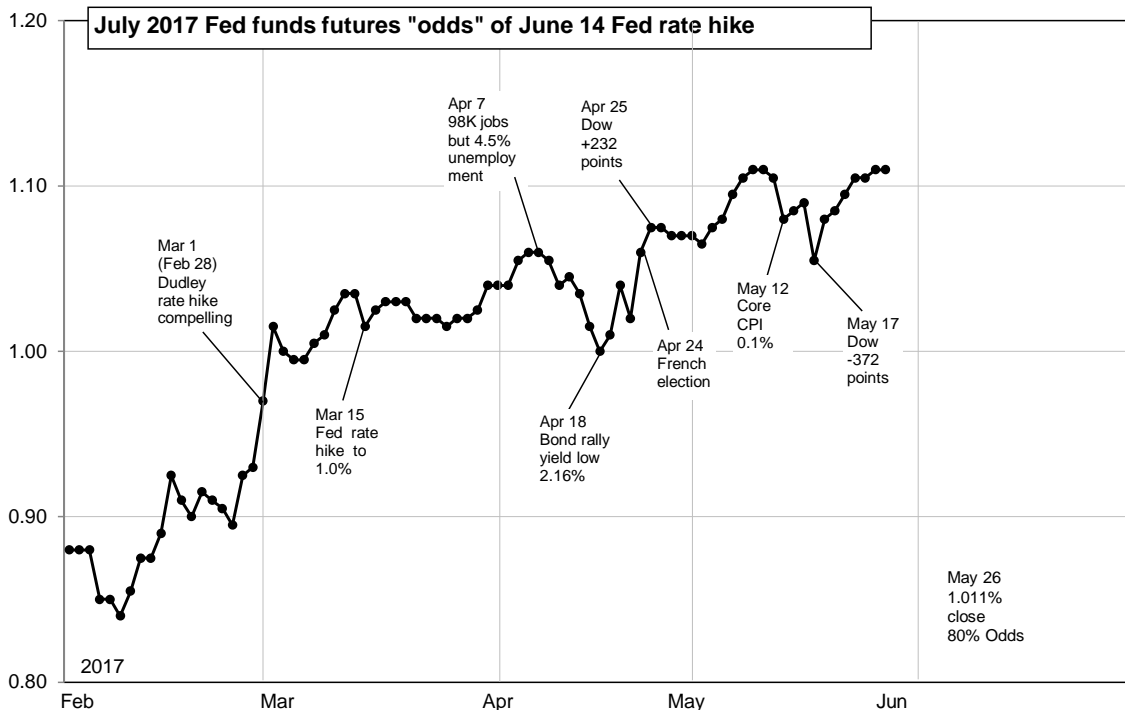
FEDERAL RESERVE POLICY

The Fed meets June 13-14 to consider its monetary policy. Yellen will hold a press conference after the meeting from 230pm to 330pm EDT, to explain the Fed's reasons behind what is widely expected to be a 25 bps rate hike in the Fed funds rate to 1.25%.

The Fed has two objectives, maximum employment which has been met, and 2.0% inflation which has not. We never understood the Fed's concern about inflation being too low; it's not as if there is any real risk of deflation as this is not an economy facing stagnation or weakened demand. We like the Fed Chair's original comment a few years ago that the Fed funds rate should be at normal when the unemployment rate comes back down to normal. Well, that condition has been met: the unemployment rate is 4.4% and it was never lower during the Greenspan housing bubble economy years of 2004 to 2006. We cannot believe the Fed funds rate isn't already up there (and not "way up there") at 3%. And keep in mind, based on their latest March FOMC meeting forecasts, the Fed funds rate will not be at 3% until the end of 2019. Too long to wait in our view, let's see what Trump's Fed Chair does with monetary policy. Time for a change.

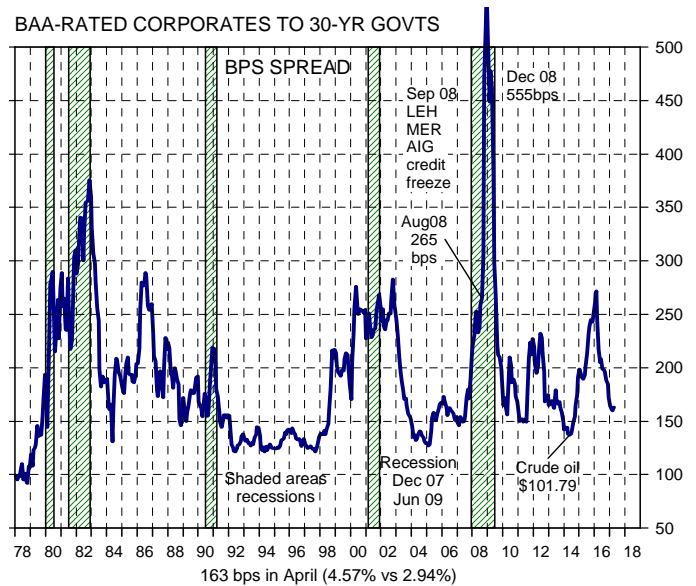
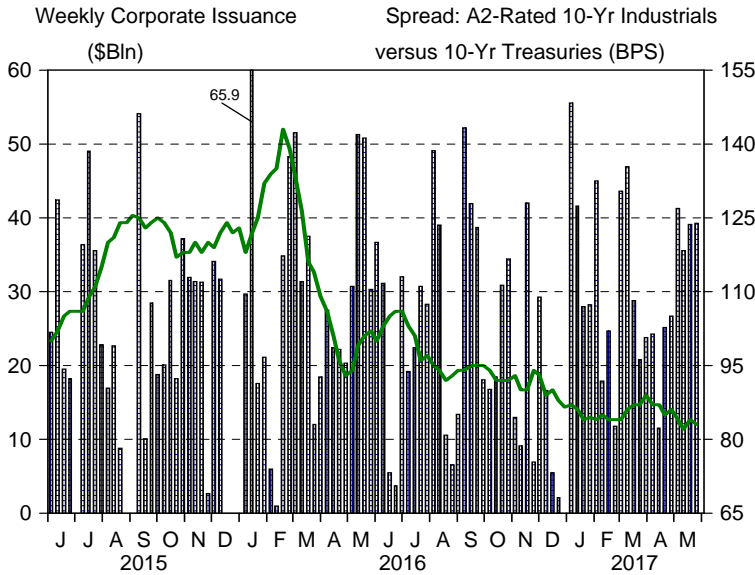
What should the Fed do on June 14 at the 2pm decision announcement time? If you ask the market, Fed funds futures traders still believe in their hearts that the odds of a 25 bps rate hike to 1.25% are 80%. July Fed funds futures closed at 1.11% on Friday, May 26, and should only move 5 bps higher to 1.16% on average in July if the Fed hikes rates.

Selected Fed assets and liabilities					Sep 10
Fed H.4.1 statistical release					2008**
billions, Wednesday data					pre-LEH
	24-May	17-May	10-May	3-May	
Factors adding reserves					
U.S. Treasury securities	2464.660	2464.638	2464.815	2464.792	479.782
Federal agency debt securities	8.834	8.834	11.829	11.829	0.000
Mortgage-backed securities	1780.383	1778.109	1769.016	1769.015	0.000
Primary credit (Discount Window)	0.011	0.023	0.000	0.024	23.455
Term auction credit (TAF auctions)	0.000	0.000	0.000	0.000	150.000
Asset-backed TALF	0.000	0.000	0.000	0.000	
Maiden Lane (Bear)	1.710	1.709	1.709	1.709	29.287
Maiden Lane II (AIG)	0.000	0.000	0.000	0.000	0.000
Maiden Lane III (AIG)	0.000	0.000	0.000	0.000	0.000
Central bank liquidity swaps	0.041	0.036	0.035	0.035	62.000
Federal Reserve Assets	4517.5	4513.6	4520.0	4517.6	961.7
3-month Labor %	1.20	1.18	1.18	1.17	2.82
Factors draining reserves					
Currency in circulation	1551.551	1548.437	1548.378	1546.200	834.477
Term Deposit Facility	16.347	0.000	0.000	0.000	0.000
Reverse repurchases w/others	184.946	167.270	187.269	186.667	0.000
Reserve Balances (Net Liquidity)	2206.163	2247.673	2219.918	2200.821	24.964
Treasuries within 15 days	11.910	11.910	20.483	20.483	14.955
Treasuries 16 to 90 days	44.608	44.608	37.862	37.862	31.549
Treasuries 91 days to 1 year	230.778	230.777	223.204	223.203	69.272
Treasuries over 1-yr to 5 years	1195.577	1195.573	1170.574	1170.570	170.807
Treasuries over 5-yr to 10 years	349.059	349.054	384.944	384.939	91.863
Treasuries over 10-years	632.730	632.716	627.747	627.733	101.337
**September 10, 2008 is pre-Lehman bankruptcy of 9-15-08					



CORPORATE BONDS: COCA-COLA, NORFOLK SOUTHERN, PUBLIC STORAGE

Corporate offerings were \$39.3 billion in the May 26 week versus \$39.1 billion in the May 19 week. On Monday, Becton Dickinson came with a \$9.7 billion 7-part offering. It priced \$2.4 billion 3.7% 10-yrs (m-w +25bp) at 145 bps (Ba1/BBB+). The global medical technology company will use the proceeds to fund its acquisition of C.R. Bard Inc. Corporate bonds (10-yr Industrials rated A2) were 83 bps above 10-yr Treasuries on Friday versus 84 bps last Friday.



TREASURY MARKET OUTLOOK

EXPECTED 10-YR 2-3 WEEK TRADING RANGE 2.00% to 2.75%

Week's 10-YR Range

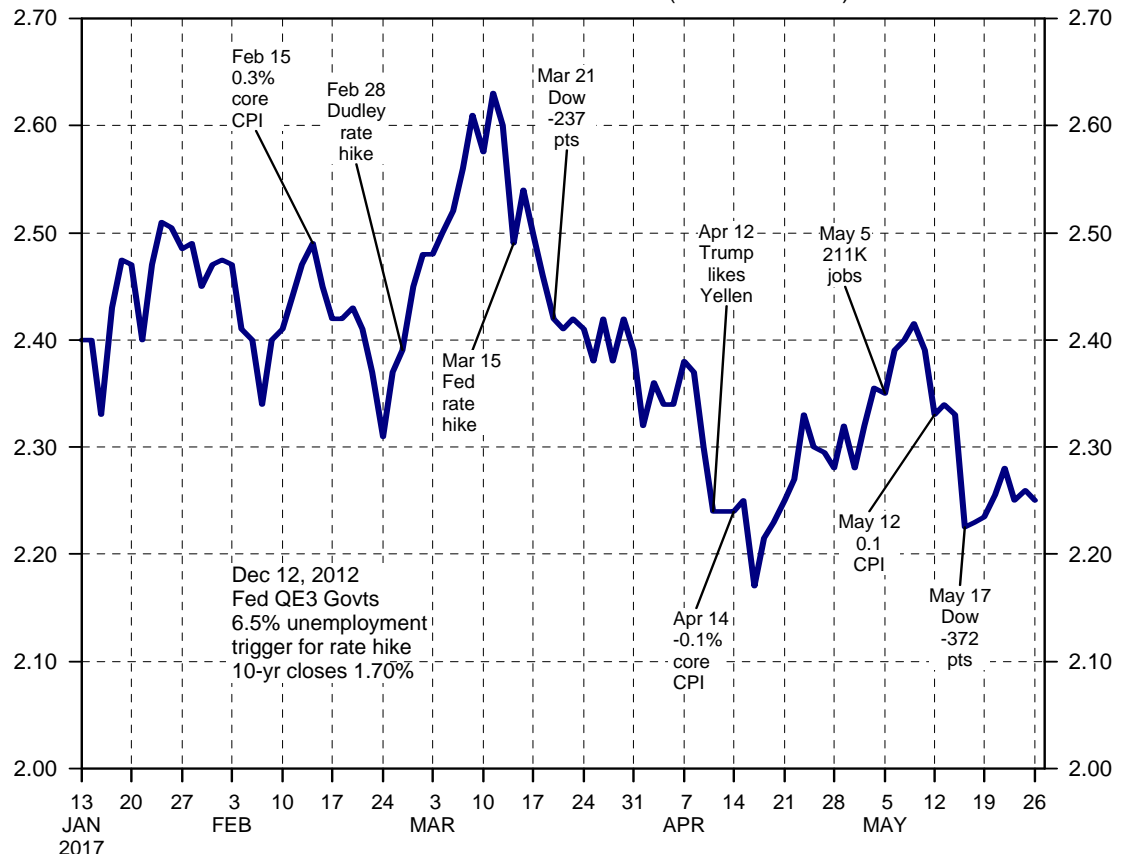
HIGH 101-11 2.22%

Tuesday, May 23, overnight highs made after U.K. terror attack in Manchester

LOW 100-22+ 2.30%

Wednesday, May 24, light selling before Fed minutes rally on tightening "soon," but not soon enough

RECENT TREND IN 10-YR GOVERNMENT NOTES (N.Y. CLOSING)



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