Financial Market Weekly

CHRISTOPHER S. RUPKEY, CFA
MANAGING DIRECTOR
CHIEF FINANCIAL ECONOMIST
ECONOMIC RESEARCH OFFICE (NEW YORK)
(212) 782-5702
crupkey@us.mufg.jp

MUFG | 1251 Avenue of the Americas
New York, New York 10020
A member of MUFG, a global financial group

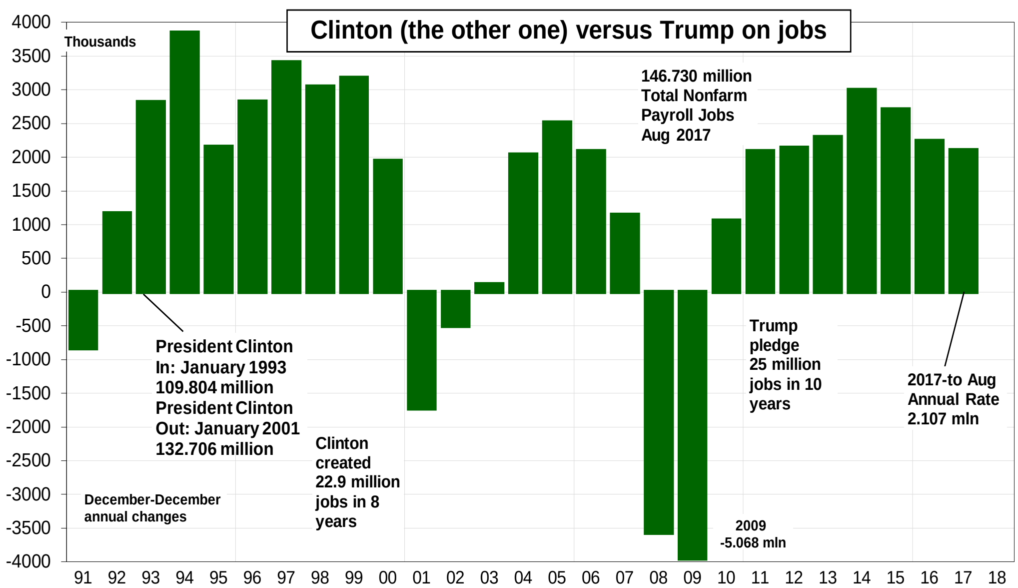
1 SEPTEMBER 2017

JOBS, JOBS, JOBS, SPECTACULAR REALLY, GREATEST EVER

Well, this week's title is what we wrote before Friday's employment report, though maybe this line is still true in some quarters. The truth is the jobs report today was on the disappointing side, so it's a good thing no one's in the office today to trade the news.

The economy has created millions of jobs without Washington's help, unless you count the Fed's zero rates policy which did a lot.

The biggest economic news report in the world, maybe next to China PMI data perhaps, will prove disappointing to all three Wall Street veterans in work today before the Labor Day holiday weekend. Those consistent 200K monthly jobs reports we were expecting have simply melted away. We thought 200K jobs today for August was possible, after June's 231K and July's 209K. Three big ones in a row. But this was not to be with: August 156K, July 189K, and June 210K. Brother can you spare a dime. Can't wait for the Washington tweet coming shortly saying "Economists tell me this was the greatest jobs report ever." I'm not going to tell him. Someone else can. We can't even blame Hurricane Harvey as the Bureau of Labor Statistics says the payroll jobs data count was "largely completed before the storm." Just wait for next month. The August 156K print will probably be revised up (August has been



	Aug	Jul	Jun	May	Apr	Mar
Payroll jobs (000s)	156	189	210	145	207	50
Unemployment rate %	4.4	4.3	4.4	4.3	4.4	4.5
Unemployment (3 decimal)	4.442	4.350	4.357	4.294	4.404	4.496
Participation rate %	62.9	62.9	62.8	62.7	62.9	63.0
Average hourly earnings	$26.39	$26.36	$26.27	$26.22	$26.18	$26.13
MTM % Chg	0.1	0.3	0.2	0.2	0.2	0.1
YOY % Chg	2.5	2.5	2.5	2.5	2.5	2.6
Production Worker earnings	$22.12	$22.08	$22.03	$21.99	$21.96	$21.90
MTM % Chg	0.2	0.2	0.2	0.1	0.3	0.2
YOY % Chg	2.3	2.3	2.3	2.4	2.3	2.3

revised higher in 14 out of the last 17 years), but the storm count in September will likely be less. Hurricane Katrina payroll jobs were -35K in September 2005 down from 196K in August 2005.

A paltry 156K the jobs count this morning. But you know what? No one cares. The Fed has sucked all the uncertainty out of the rates forecast anyway with its extended guidance for the path of rates over the next couple of years ending way out there in December 2019. There are no traders worth their salt in work today to trade the news. Dow industrials stock futures were +65 points and 10-yr yields were 2.12% before the soft employment report, and 15 minutes later stocks are up 60 points and 10-yr yields are unchanged at 2.12%.

The other two main components of the employment report were just as unspectacular. Unemployment rate up a tenth to 4.4% (just missed 4.5% at 4.442 three-decimal count), and average hourly earnings up just 0.1%, although it held at the same 2.5% year-on-year rate of change. That's right workers. Management values your productivity contribution so highly that they gave you three more cents this month in your paycheck, your hourly wage rising from $26.36 in July to $26.39 in August. Brother can you spare a dime. No. They can't. Three cents only.

As far as the 156K August increase in payroll jobs itself, it seems to be boosted this month by an above trend 28K jump in construction jobs, must be those specialty contractors in their trucks up and down my street, and another large increase in manufacturing jobs. Maybe those factories are coming back to the good old USA after all. Manufacturing jobs up 21K in June, 26K in July, and 36K in August. Who is hiring? Fabricated metal products again, up 5.2K this month, Computers/electronic products up 3.9K, Motor vehicles and parts +13.7K, Food manufacturing +6.6K, and Plastics and rubber products up 2.6K, so you college graduates, make sure to get your resumes in there: "Plastics."

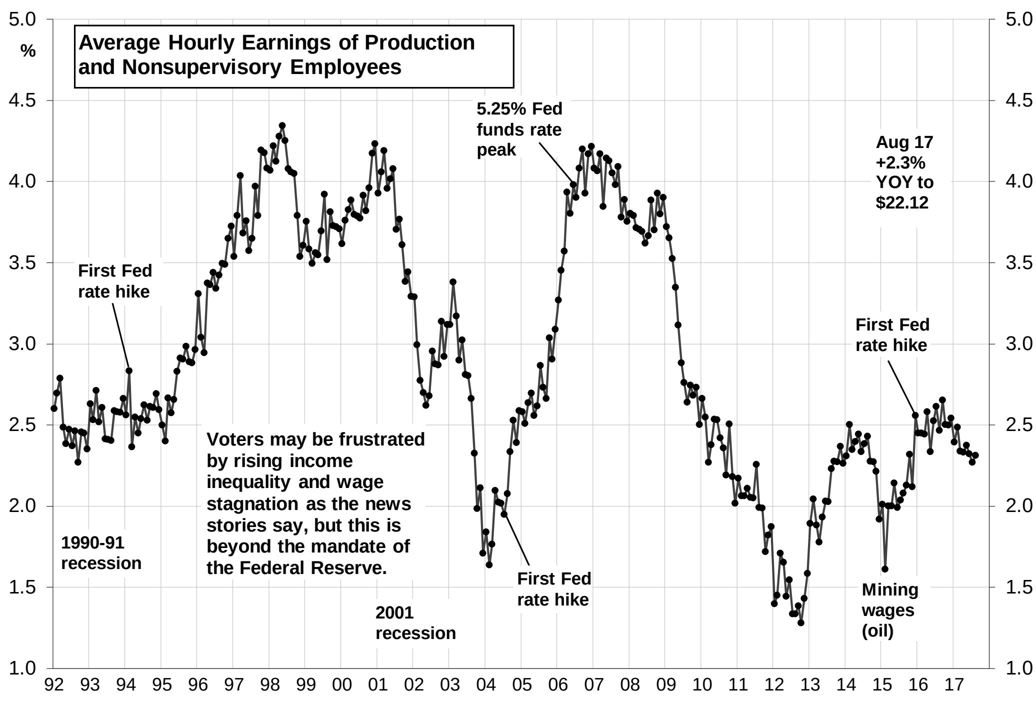
Payroll jobs in year nine following the recession

Dec. 2016 Totals millions		Aug 17	Jul 17	Jun 17	8 months Dec 16 to Aug 17	12 months Dec 15 to Dec 16
145.325	Nonfarm Payroll Employment	156	189	210	1405	2240
123.026	Total Private (ex-Govt)	165	202	207	1406	2039
19.794	Goods-producing	70	23	42	323	64
0.617	Mining	7	2	6	54	-75
12.343	Manufacturing	36	26	21	137	-16
0.942	Motor Vehicles & parts	14	5	3	23	17
6.783	Construction	28	-3	15	135	155
103.232	Private Service-providing	95	179	165	1083	1975
27.374	**Trade, transportation, utilities**	8	5	15	16	331
15.881	Retail stores	1	-2	-4	-52	203
3.180	General Merchandise	3	7	6	-43	37
3.097	Food & Beverage stores	-1	-3	-2	-20	37
5.048	Transportation/warehousing	2	2	6	29	92
1.465	Truck transport	-2	1	-1	6	10
0.668	Couriers/messengers	4	3	4	5	31
0.943	Warehousing and storage	1	-2	2	8	63
0.557	Utilities	-1	-1	1	-4	0
2.762	**Information**	-8	-4	-1	-51	0
8.364	**Financial**	10	10	15	100	176
2.605	Insurance	0	3	-2	21	46
2.169	Real Estate	7	-2	7	32	59
1.311	Commercial Banking	0	0	1	8	17
0.933	Securities/investments	-1	4	4	16	18
20.416	**Professional/business**	40	50	44	382	534
2.962	Temp help services	0	10	11	76	32
2.259	Management of companies	0	4	6	25	35
1.427	Architectural/engineering	4	2	5	37	27
2.032	Computer systems/services	8	5	4	35	87
1.126	Legal services	0	-5	3	0	5
1.000	Accounting/bookkeeping	2	3	0	7	32
22.871	**Education and health**	25	54	40	302	553
5.077	Hospitals	6	7	12	48	119
3.604	Educational services	9	10	-10	35	85
15.744	**Leisure and hospitality**	4	58	38	252	331
1.950	Hotel/motels	-2	-1	3	8	11
11.549	Eating & drinking places	9	53	20	213	276
22.299	Government	-9	-13	3	-1	201
2.200	Federal ex-Post Office	0	-2	0	-9	30
5.085	State government	-5	-2	-1	-2	-4
2.414	State Govt Education	-3	-1	-3	7	3
14.395	Local government	-3	-10	5	12	160
7.945	Local Govt Education	0	-16	-5	-8	69

Net, net, the monthly employment report is disappointing today even if the jobs undercount occurs frequently in August each year for varying reasons. Trump's economics team will have to redouble their efforts. That campaign pledge to create 25 million jobs over the next decade will be a tall order for this new Administration. For the Fed officials, their assessment of today's report will be strictly, where there's smoke there's fire, at least for those officials already questioning the economy's underlying strength given the soft patch inflation reports the last several months. They will tell the others on the Federal Open Market Committee, "See, we told you so." The slowdown in jobs creation shows the economy is not throwing off enough sparks of faster growth to wake the inflation genie slumbering in his lamp. We wish it weren't true, but the payroll jobs count is simply not great enough to put a September rate hike back on the table; but we do still expect policymakers to officially announce the start of the balance sheet wind down later this month. It's supposed to run silently in the background doing nothing anyway.

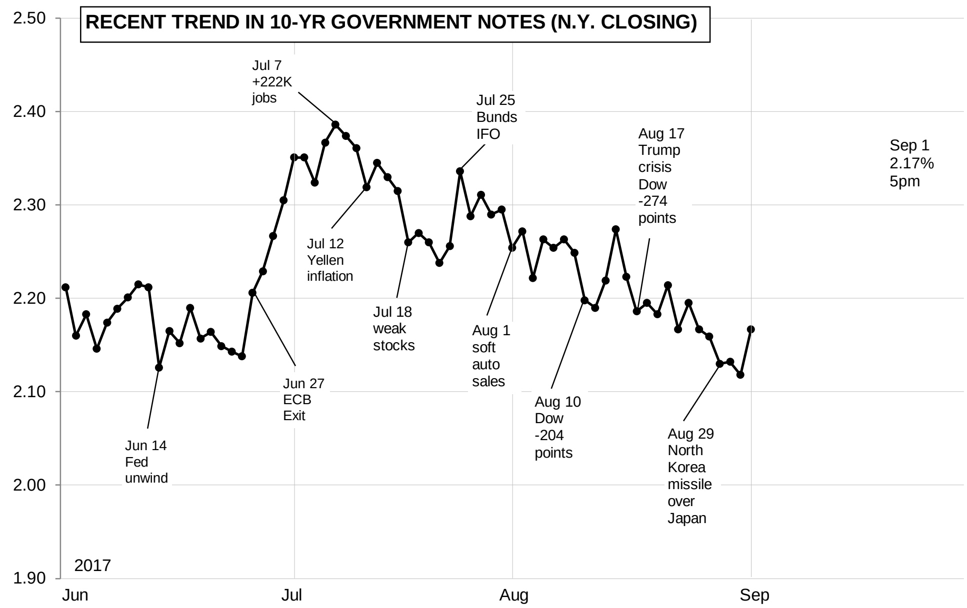
What does it all mean? Fed officials thought jobs growth would slow this late in the cycle anyway given the expansion's advanced age. It is all starting to make sense in a sense. 250K jobs per month in 2014, 226K jobs per month in 2015, 187K jobs per month in 2016, and 176K jobs per month so far in 2017. Don’t quibble over whether jobs are truly 156K rather than the 180K consensus forecast. The die is cast. Job creation will continue to slow. The economy can't create more jobs as there is no one left to hire at this late stage of the recovery with the expansion starting its ninth year in July. Today's report is likely to be the new normal for jobs growth on a sustained basis going forward. The economy is completely back to normal and it is only the Federal Reserve that is not back to normal. Stay tuned.

Stagnant 2.3% working-man wages probably stuck as many companies index annual wage rates to CPI inflation (1.7% last)



MARKETS OUTLOOK

	30-Jun 2017	Q3 2017	Q4 2017	Q1 2018	Q2 2018	Q3 2018	Q4 2018	Q1 2019	Q2 2019	Q3 2019	Q4 2019
30-Yr Treasury	2.83	3.10	3.20	3.40	3.60	3.70	3.80	4.00	4.10	4.10	4.10
10-Yr Note	2.30	2.50	2.70	3.00	3.20	3.40	3.50	3.70	3.80	3.90	3.90
5-Yr Note	1.89	2.10	2.40	2.70	3.00	3.20	3.30	3.50	3.60	3.70	3.70
2-Yr Note	1.38	1.60	1.85	2.10	2.40	2.60	2.85	3.10	3.35	3.35	3.60
3-month Libor	1.30	1.65	1.90	2.20	2.45	2.70	2.95	3.20	3.45	3.35	3.70
Fed Funds Rate	1.25	1.50	1.75	2.00	2.25	2.50	2.75	3.00	3.25	3.25	3.50
2s/10s spread	92	90	85	90	80	80	65	60	45	55	30
Libor/funds spd	5	15	15	20	20	20	20	20	20	10	20



The bond rally from “2.40%” in early July extended itself overnight Tuesday (well, 5:17pm NY time on Monday) on news of a North Korea missile being shot over Japan. Yields fell as low as 2.08% by 4am EDT Tuesday morning here. The employment report reaction on Friday was interesting even if few were in the office to witness it. Yields were 2.12% at the 156K softer payroll jobs 830am release time, and fell haltingly only a couple of basis points to 2.10% before moving back up. A Bloomberg news story at 840am about the ECB unlikely to formalize plans before December to scale back QE helped. And believe or not, at 10am the ISM Manufacturing index jumped 2.5 points to a 2017 high of 58.8, news which somehow sent yields higher even though payroll jobs is the more important indicator. Call it a week then. 10-yr yields closed at 2.17%.

FEDERAL RESERVE POLICY

The Fed meets September 19-20 to consider its monetary policy. A rate hike doesn’t seem very likely, but we won’t stop forecasting one. The Fed inflation mongers are talking like they won’t even vote to hike rates in December if inflation does not pick up. Let’s see core PCE inflation is 1.4% and core CPI inflation is 1.7%, and the Fed is somehow trying to convey to the public that this “low inflation” is unacceptable and that business and economic conditions are not fully healed or something worse: stagnation and weak demand are causing the drop in inflation. Another reason not to return rates to normal pre-recession levels.

Selected Fed assets and liabilities					Sep 10
Fed H.4.1 statistical release					2008**
billions, Wednesday data	30-Aug	23-Aug	16-Aug	9-Aug	pre-LEH
Factors adding reserves					
U.S. Treasury securities	2465.300	2465.273	2465.247	2465.221	479.782
Federal agency debt securities	6.757	6.757	8.097	8.097	0.000
Mortgage-backed securities	1767.553	1778.699	1777.975	1769.029	0.000
Primary credit (Discount Window)	0.004	0.005	0.002	0.001	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)	1.708	1.708	1.708	1.710	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	0.036	0.036	0.036	0.036	62.000
Federal Reserve Assets	4498.4	4510.5	4509.8	4515.8	961.7
3-month Libor %	1.32	1.32	1.32	1.31	2.82
Factors draining reserves					
Currency in circulation	1570.551	1566.641	1566.526	1567.095	834.477
Term Deposit Facility	0.000	0.000	14.733	0.000	0.000
Reverse repurchases w/others	146.086	169.793	92.840	103.950	0.000
Reserve Balances (Net Liquidity)	2331.956	2338.169	2364.971	2336.315	24.964
Treasuries within 15 days	3.197	3.197	3.197	18.655	14.955
Treasuries 16 to 90 days	30.691	30.691	19.648	22.845	31.549
Treasuries 91 days to 1 year	310.316	310.315	321.357	298.287	69.272
Treasuries over 1-yr to 5 years	1163.518	1163.479	1163.475	1129.964	170.807
Treasuries over 5-yrs to 10 years	324.365	324.394	312.184	361.534	91.863
Treasuries over 10-years	633.213	633.197	645.386	633.937	101.337

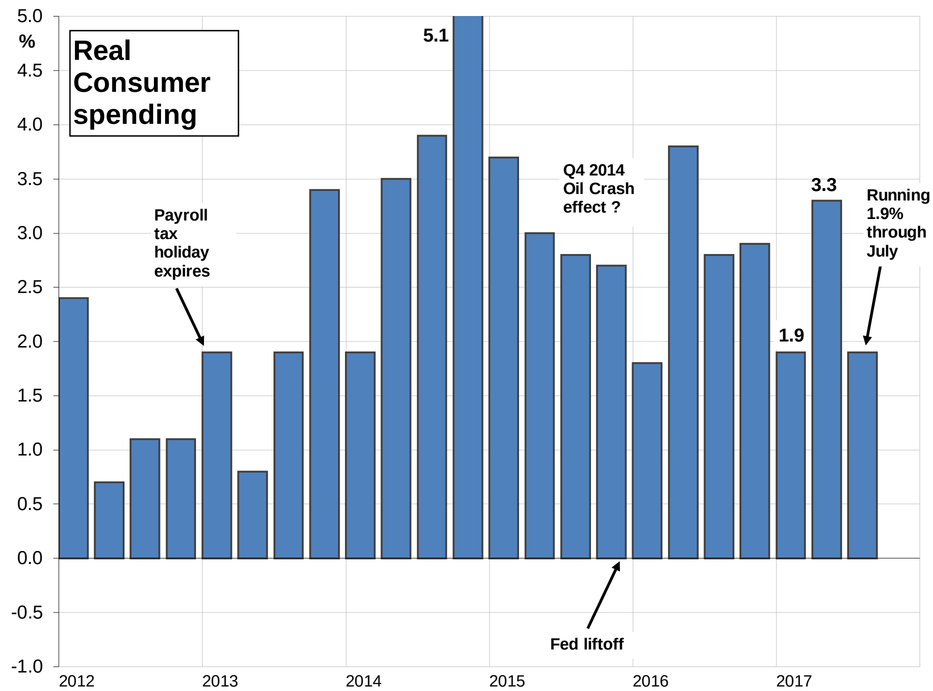
**September 10, 2008 is pre-Lehman bankruptcy of 9-15-08

OTHER ECONOMIC NEWS THIS WEEK

Consumer powers economy forward in Q3, core inflation short at 1.4%

Breaking economy news. The monthly personal income report and weekly jobless claims.

Jobless claims were little changed at full employment levels of 236K in the August 26 week. This measure showing labor market tightness stands in stark contrast to the Trump administration view that its economic policies need to be geared to producing more jobs, jobs, jobs. Not going to happen if you don't bring those factories back from overseas. The reality is the labor market cannot be pushed any tighter and that labor is in short supply especially for skilled workers. How the economy continues to add over 200K new workers each month is increasingly hard to explain given the widespread worker shortages in this the ninth year of an economic expansion that is showing some signs of age.

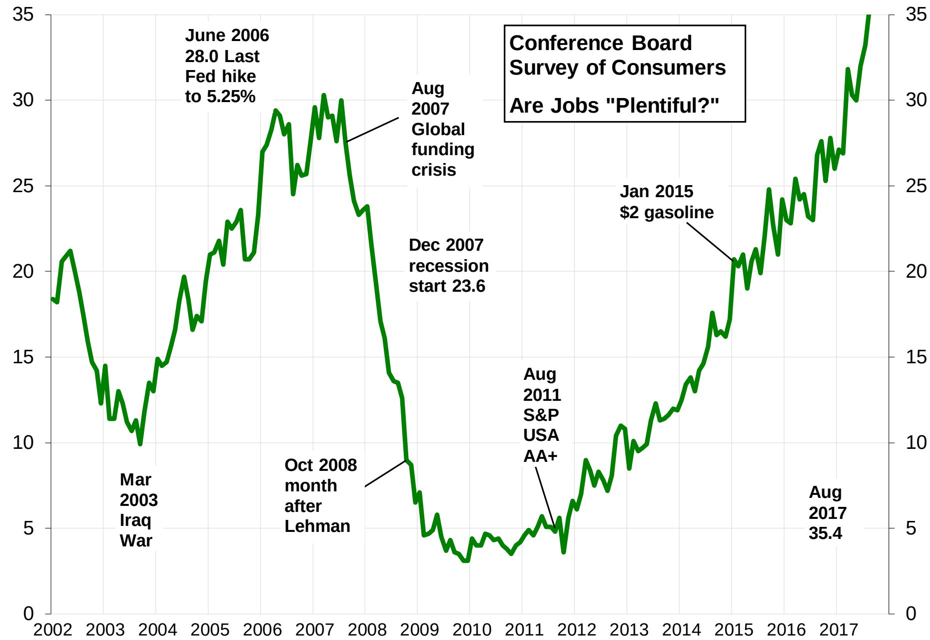


Consumer spending looks rock solid. Yesterday consumption expenditures were revised up in the second quarter to a fast-paced 3.3% from the preliminary estimate of 2.8%. This is the second year in a row where soft spending in the first "winter" quarter of the year bounced back strongly in the following quarter. The key question is whether consumption will continue at such a strong pace and here consumer spending in the third quarter is doing well, rising 1.9% with data in just for July so far.

Net, net, the consumer continues to do the heavy lifting when it comes to economic growth as corporations hold back investment plans until they see what tax reform proposals make it through Congress. The consumer's got the money with personal income jumping 0.4% in July and they are spending it. The growth outlook has brightened from this time last month as consumer spending is moving at a faster pace. Growth looks fine and we will hold with our 2.8% forecast for the third quarter real GDP report due out on October 30. Inflation looks less fine and will likely be a concern of those Fed officials wanting to hold back on rate hikes lest it slow the economy until inflation shows signs of strengthening. Inflation remains in a slow patch with today's 0.1% increase in the month of July, the third consecutive month where the monthly change is just 0.1%. Inflation is in the slow lane for now and this is likely to make Fed officials cautious on the need to raise rates a third time this year. The full committee has foreseen three rate hikes in 2017 since last December so taking the final one off the table would be a big deal. Stay tuned. Story developing.

Sure, Confidence bounces back, but for how long?

Breaking economy news. Consumer conference bounces back in August to 122.9 from a downward revised 120.0 in July now. The consumers fortunes are definitely looking up a bit right now in August late in the summer but you have to you have to scratch your head and ask yourself for how long? The true state of that huge natural disaster down there in the Gulf in the city of Houston the extent of the damage and loss of life still is unknown. And with the disaster in the making overseas in North Korea, where the President says all options are open, who knows how long consumer confidence is going to hang in there. Hurricane Katrina back this time of year in 2005 almost made the Federal Reserve skip one of their famous 17 in a row rate hikes. It was that bad. Hurricane Harvey reminds us potentially of another Hurricane Katrina hit to the economy. In terms of consumer confidence.



We are glad that we left our nonfarm payroll jobs estimate for Friday at 200,000 which would mean three months in a row of 200,000 monthly jobs because in today's report the number of people saying that jobs are plentiful is soaring into the stratosphere. 33.2% in July and now 35.4% say jobs are plentiful and jobs are everywhere for the taking in the month of August which could bode well for a big jobs number on Friday and put potentially another rate hike back on the table for the Federal Reserve later on this year. All clear for now despite the storm clouds potentially on the horizon for the Federal Reserve and they can continue with their policy of gradually removing the accommodation from the recession and continue to move policy back towards more normal levels. Stay tuned though, story developing.

Analyst Certification

The views expressed in this report accurately reflect the personal views of **Christopher S. Rupkey**, the primary analyst responsible for this report, about the subject securities or issuers referred to herein, and no part of such analyst's compensation was, is or will be directly or indirectly related to the specific recommendations or views expressed herein.

About MUFG Americas Holdings Corporation

Headquartered in New York, MUFG Americas Holdings Corporation is a financial holding company and bank holding company with total assets of $148.1 billion at December 31, 2016. Its main subsidiaries are MUFG Union Bank, N.A. and MUFG Securities Americas Inc. MUFG Union Bank, N.A. provides an array of financial services to individuals, small businesses, middle-market companies, and major corporations. As of December 31, 2016, MUFG Union Bank, N.A. operated 365 branches, comprised primarily of retail banking branches in the West Coast states, along with commercial branches in Texas, Illinois, New York and Georgia, as well as two international offices. MUFG Securities Americas Inc. is a registered securities broker-dealer which engages in capital markets origination transactions, private placements, collateralized financings, securities borrowing and lending transactions, and domestic and foreign debt and equities securities transactions. MUFG Americas Holdings Corporation is owned by The Bank of Tokyo-Mitsubishi UFJ, Ltd. and Mitsubishi UFJ Financial Group, Inc., one of the world’s leading financial groups. The Bank of Tokyo-Mitsubishi UFJ, Ltd. is a wholly owned subsidiary of Mitsubishi UFJ Financial Group, Inc. Visit http://www.unionbank.com/ or http://www.mufgamericas.com/ for more information.

About MUFG (Mitsubishi UFJ Financial Group, Inc.)

MUFG (Mitsubishi UFJ Financial Group, Inc.) is one of the world’s leading financial groups, with total assets of approximately $2.6 trillion (USD) as of December 31, 2016. Headquartered in Tokyo and with approximately 350 years of history, MUFG is a global network with more than 2,200 offices in nearly 50 countries. The Group has more than 140,000 employees and about 300 entities, offering services including commercial banking, trust banking, securities, credit cards, consumer finance, asset management, and leasing. The Group’s operating companies include Bank of Tokyo-Mitsubishi UFJ, Mitsubishi UFJ Trust and Banking Corporation (Japan’s leading trust bank), and Mitsubishi UFJ Securities Holdings Co., Ltd., one of Japan’s largest securities firms.

Through close partnerships among our operating companies, the Group aims to "be the world’s most trusted financial group," flexibly responding to all of the financial needs of our customers, serving society, and fostering shared and sustainable growth for a better world. MUFG’s shares trade on the Tokyo, Nagoya, and New York (MTU) stock exchanges. Visit www.mufg.jp/english/index.html.