

3rd Quarter 2015plante moran
FINANCIAL ADVISORS

EXECUTIVE SUMMARY

- The most recent report on Q2 GDP indicated that the economy expanded at a healthy 3.9% annualized rate during the quarter. Growth was supported by stronger consumer and government spending, business investment, and inventory accumulation. Q1 GDP was also revised up from -0.2% to 0.6%.
- Recent inflation data has been muted, as commodity prices remain depressed. Headline CPI increased a mere 0.2% in August on a year-over-year basis. Core CPI, which excludes food and energy, increased at a rate of 1.8%, in line with the month prior.
- Long-term interest rates remained volatile during the third quarter, as investors digested news out of China and speculated about the timing of rate hikes. The 10-year Treasury yield ended September at 2.06%, down fractionally for the quarter.
- The September jobs report was undeniably disappointing as payrolls rose by only 142,000, and gains for July and August were revised downward. On a brighter note, the unemployment rate held steady at 5.1% – its lowest point in over seven years.
- The U.S. economy is slowing, but still appears to be expanding at a moderate pace. However, recent data out of China has prompted a softening of expectations for global growth, as the structural tailwind that was provided by the rapid growth pace of many emerging market countries has faded.



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Economic Dashboard

Gross Domestic Product	Prior Reading	Change	Most Recent
Real GDP QoQ - Q2 (III Est.)	0.6%	↑	3.9%
Personal Consumption QoQ - Q2 (II Est.)	1.8%	↑	3.6%
Employment Market			
Unemployment Rate - September	5.1%	↔	5.1%
Nonfarm Payrolls (Change) - September	136K	↑	142K
Initial Jobless Claims 4-Week Avg - September	271.8K	↓	270.8K
Continuing Jobless Claims 4-Week Avg - September	2252.3K	↓	2235.3K
Inflation			
CPI YoY - August	0.2%	↔	0.2%
Core CPI YoY - August	1.8%	↔	1.8%
Core PCE YoY - August	1.2%	↑	1.3%
Consumer Indicators			
Retail Sales YoY - August	2.6%	↓	2.2%
Consumer Credit YoY - July	6.9%	↓	6.8%
Personal Income YoY - August	4.3%	↓	4.2%
Personal Savings YoY - August	4.7%	↓	4.6%
Consumer Confidence - September	101.3	↑	103.0
Business & Production Indicators			
ISM Manufacturing Index - September	51.1	↓	50.2
ISM Services Index - August	60.3	↓	59.0
Industrial Production YoY - August	1.3%	↓	0.9%
Small Business Optimism - August	95.4	↑	95.9
Housing Market			
Existing Home Sales - August	5.58MM	↓	5.31MM
Housing Starts - August	1161K	↓	1126K
S&P Case-Shiller Price Index YoY - July	4.9%	↑	5.0%
Leading Indicators			
ECRI Weekly Leading Index - September	130.9	↑	131.1
Conference Board Leading Economic Index - August	123.6	↑	123.7

OVERVIEW

Keeping a continuous pulse on the growth rate of an economy has never been an easy task. In the U.S., the Bureau of Economic Analysis only releases quarterly estimates for gross domestic product (GDP) growth, the predominant measure of economic growth. However, initial estimates are subject to further revisions for several years as more complete source data becomes available. Moreover, the National Bureau of Economic Research (NBER), a nonprofit organization that monitors economic conditions broadly and serves as the official arbiter of the U.S. business cycle (calling the start of both recessions and expansions), typically cannot declare a turning point in the economy for several quarters, or sometimes over a year, after the fact. *At times, their official recession call has come after the recession has ended and the economy is growing again.* Gaining a real-time picture of the current economic landscape is – at best – a challenging task.

Since GDP is a lagging gauge on the health of the economy, strategists and economists tend to gravitate to more timely measures of the economic environment, not only here in the U.S., but globally as well. Other data and statistics, particularly

those which will impact the underlying measurement of GDP, are often used to evaluate both current and potential future economic conditions.

One example is the Markit Purchasing Managers' Index (PMI), which collects survey data from purchasing managers across the manufacturing sector. Although its contribution to GDP has declined over the last few decades, its cyclicity makes manufacturing sector a key leading indicator of economic growth. A PMI reading of 50 or higher typically indicates an expanding manufacturing sector, while a reading lower than 50 is viewed as contractionary.

Historically, when the manufacturing sector exhibits a sustained trend of expansionary or contractionary readings, the overall economy would be expected to follow suit. As the chart below illustrates, the recent trends in global manufacturing data across most developed countries remain constructive, as the major regional indices are all above the threshold level of 50.

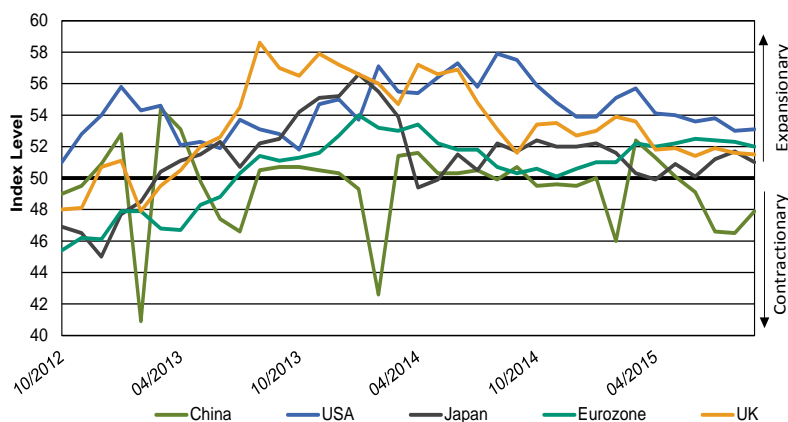
Meanwhile, China's PMI has delivered contractionary readings in recent months, prompting concerns of a hard landing for the Chinese

economy. Weaker growth in China, falling commodity prices, and a stronger U.S. dollar have contributed to a selloff in emerging-market equities and have been key drivers of heightened risk aversion globally.

Although the strength of recent PMI readings within the U.S. have softened, the manufacturing sector in the U.S. is still expanding modestly. Other economic indicators also support expectations for positive, albeit moderating, economic growth in the coming quarters. Labor market conditions remain generally favorable, as jobless claims remain quite low and nonfarm payrolls continue to expand. Consumer sentiment has dipped in recent months but remains broadly positive, supporting continued growth in consumer spending. Core inflation remains low but should edge higher as energy prices stabilize.

While concerns over slower global growth has risen in recent months and does create some risk, the full impact of that slowdown on the U.S. and other developed countries remains to be seen. To this point, a broad range of data suggests that the U.S. economy has decelerated after a strong second quarter but remains on a moderate growth path.

DEVELOPED ECONOMIES REMAIN IN EXPANSIONARY TERRITORY



Source: PMFA, Federal Reserve, Markit

INSIGHTS

Manufacturing conditions have been solid in the U.S. and other developed regions for most of the past three years since crossing into expansionary territory in the Eurozone, U.K., and Japan in 2013. The outright contraction in Chinese manufacturing in recent months has weighed on global growth estimates and stoked concerns about the ripple effect of the broader slowdown of emerging market economies in the U.S. and other developed economies – particularly those more reliant upon Chinese imports.

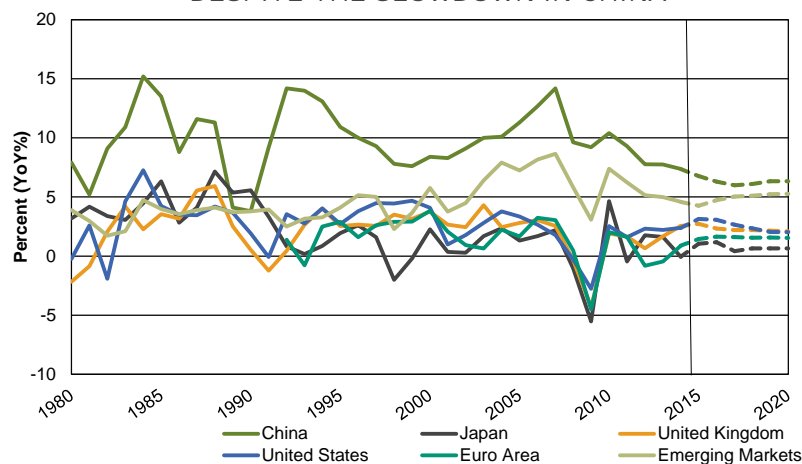
Thus far, recent PMI data suggests that the manufacturing sector in developed countries has continued to expand, although the pace of growth has slowed.

GROSS DOMESTIC PRODUCT

	Q4 Final	Q1 Final	Q2 II Est.
Real GDP QoQ	2.1%	0.6%	3.9%
Personal Consumption QoQ	4.3%	1.8%	3.6%

- The U.S. economy expanded at a 3.9% annualized rate during the second quarter, as the most recent estimates suggested that Q1 and Q2 GDP growth was stronger than initially thought.
- Consumer spending, which remains the largest driver of the U.S. economy, expanded at a 3.6% rate during Q2. A strengthening labor market, cheaper gasoline, and rising home prices likely contributed to rising optimism and an increased willingness to spend.
- Slowing growth in China and other emerging economies has driven a moderation in global growth expectations. Emerging markets are still projected to grow more rapidly than developed economies, although that gap has narrowed. Growth rates for the Euro area and U.K. are projected to converge with the U.S. over the next five years.

GLOBAL GROWTH CONTINUES TO GROW MODESTLY DESPITE THE SLOWDOWN IN CHINA



International Monetary Fund (IMF) Projections past 2014

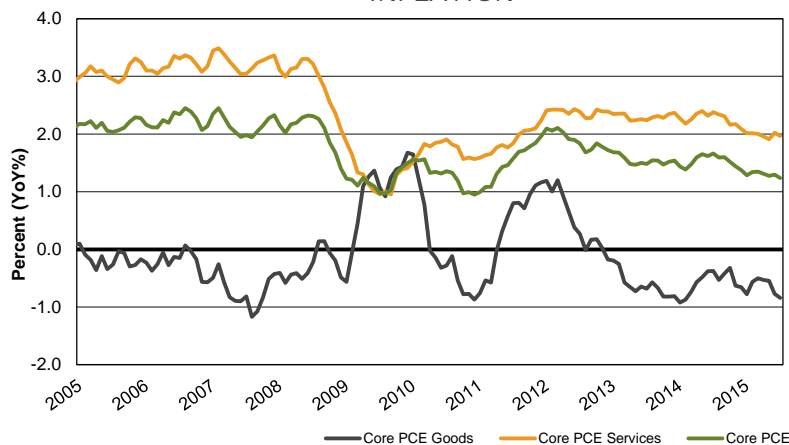
Source: PMFA, International Monetary Fund

INFLATION

	June	July	August
Consumer Price Index YoY	0.1%	0.2%	0.2%
Producer Price Index YoY	-0.7%	-0.8%	-0.8%

- The Consumer Price Index decreased by 0.1% in August but rose by a mere 0.2% on a year-over-year basis. Core inflation edged higher by a modest 0.1% during the month.
- Weakness in energy prices continue to have a disinflationary effect on headline inflation. Over the trailing 12 months, all major energy components have declined. While the electricity index has fallen just 0.6%, the index for gasoline is down more than 23%.
- Core PCE – the Fed's preferred measure of inflation – has remained below the central bank's goal of 2% since April 2012. As the chart illustrates, the price level for core services has been increasing at a steady rate for the last several years, suggesting that weakness in core PCE has instead been driven by the deflationary trend in core goods. The price of goods, particularly durable goods, has been impacted by a strengthening U.S. dollar and, more recently, falling oil prices.

A LARGE GAP BETWEEN SERVICE AND GOODS INFLATION



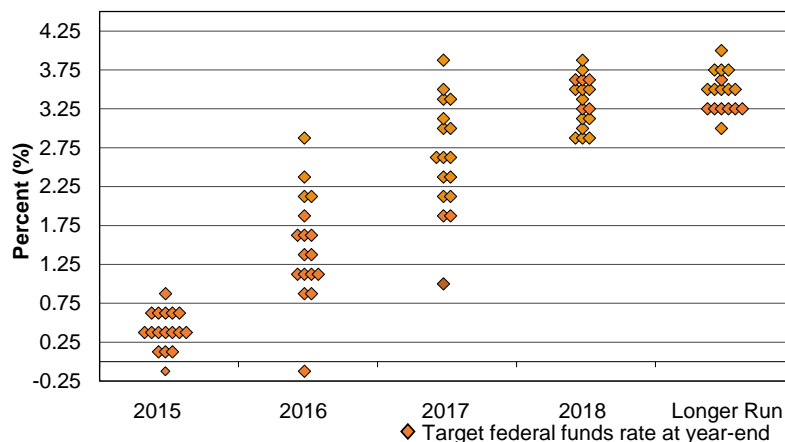
Source: PMFA, Bureau of Economic Analysis

INTEREST RATES

Treasury Yields as of	9/30/14	3/31/15	9/30/15
3-month	0.02%	0.03%	0.00%
2-year	0.58%	0.56%	0.64%
10-year	2.52%	1.94%	2.06%

- Long-term interest rates trended downward during the quarter as continued equity market volatility drove a flight to quality. After testing the 2.0% level in August and September, the 10-year Treasury yield ended the quarter at 2.06%.
- At the September FOMC meeting, the Fed once again left short-term interest rates unchanged, citing recent global economic and financial developments as potential headwinds to U.S. growth and inflation.
- The FOMC statement and updated “dot plot” (see chart on right) once again carried a more dovish tone than many expected, but left the door open for a rate hike later this year. In fact, the majority of FOMC members still expect the first rate hike since 2006 to occur by year end, with all but one anticipating the federal funds rate above 0.75% by the end of 2016.

FED FUNDS RATE REMAINS ON HOLD



Note: Each diamond indicates the value (rounded to the nearest 1/8 percentage point) of an individual participant's judgment regarding the appropriate level of the federal funds rate at the end of the specified calendar year or over the longer run.

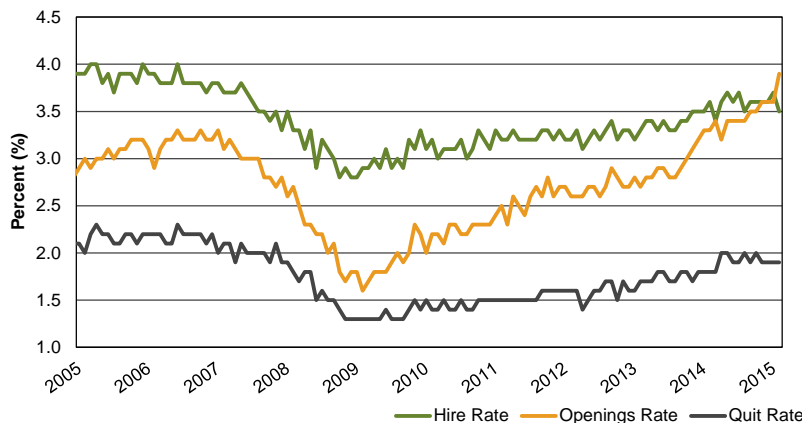
Source: PMFA, Federal Reserve

EMPLOYMENT

	July	August	September
Unemployment Rate	5.3%	5.1%	5.1%
Nonfarm Payrolls (Change)	223K	136K	142K

- The labor market has been a bright spot in the U.S. economy but has lost some luster on the back of the disappointing September jobs reports. Nonfarm payrolls increased by 142,000 in September, but the accompanying revisions to prior months limited the net increase for the month to a mere 83,000.
- The unemployment rate was unchanged at 5.1% in September – the lowest reading in over seven years. While labor force participation has been declining, the number of unemployed persons has fallen by 1.3 million over the last year.
- Other gauges of labor market health also tell a positive story. Since 2009, the hiring rate has trended upward and currently sits above 3.5%, near its cyclical peak. The job openings rate surged to a record high in July, eclipsing the rate of hiring, even as the quit rate edges higher, as more workers have gained confidence to seek out a better job. Wage growth remains limited, but an increasingly competitive environment for employers should support stronger wage growth as labor conditions continue to tighten.

JOB OPENINGS SURGE TO RECORD HIGH IN JULY



Source: PMFA, Bureau of Labor Statistics

Past performance does not guarantee future results. All investments include risk and have the potential for loss as well as gain.

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Sources for the Economic Dashboard include PMFA, Bureau of Economic Analysis (BEA), Bureau of Labor Statistics (BLS), U.S. Department of Labor, U.S. Census Bureau, Federal Reserve, The Conference Board, Institute for Supply Management (ISM), National Federation of Independent Business (NFIB), U.S. Department of Housing and Urban Development, National Association of Realtors, Standard & Poor's (S&P), and the Economic Cycle Research Institute (ECRI).

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