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BOND MARKET REVIEW

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Fantastic Four

The revision of second–quarter U.S. GDP from 2.30% to 3.70% makes you want to believe things are improving nicely. Other data keeps one suspect! The Fed's Beige Book showed similar language to reports over recent years. Six districts said growth was *"moderate"*, while five said growth was *"modest."* If GDP was nearly a fantastic 4%, shouldn't at least one of the 12 districts have reported growth as 'stellar', or at least something beyond the M&Ms we've seen for years? The slowdown in China was mentioned as causing weaker demand numerous times in the report. Actually, China's factory gauge just fell to its lowest level in 3 years, and China has eased rates now 5 times since November. Focusing only on jobs and this GDP release, and not on the global stock selloff, a few Fed members have said the economy is healthy enough to begin to remove accommodation. There are a few things to consider. The International Monetary Fund also called global growth *"moderate"* and just said downside risks have increased. They said central banks *"must stay accommodative"*, warning that some of their scenarios might imply a *"much weaker outlook."* Moody's Investor Service cut 2016 G20 growth forecasts. Moreover, Canada may have entered a recession – and as our #1 export market, pose more of a threat to U.S. growth than China.

Trainwreck

The Dow surged 619.07 points last Wednesday and 369.26 points last Thursday for the largest 2–day advance since 2008. Those gains and a 500–point rally off Monday's (08/24) early 1,089.42–point loss actually left the Dow ahead 186.26 points for the week of the 28th. That said, even after a near 300–point rally today, the Dow is still over 1,200 points off its last swing high made on August 18th – the day before the release of July's FOMC minutes. It's also 2,000 points off its May 19th high, though it had been nearly 3,000 points below that high the morning of August 24th. It was an ugly August with the Dow losing 1,161.83 points or 6.57%. The S&P dropped 6.26% and the Nasdaq lost 6.86%. The Japanese Nikkei lost 8.23%, and Germany's DAX fell 9.28%. China's markets fell over 12%. While the Dow had its worst monthly loss in 5 years and China's markets fell the most since 2008, it was the worst month overall for global equities since May 2012. The *"larger cyclic low due in early September"* we've expected since the **BMR** (07/22) appears to have played out to script. Our larger cycles now show a cyclic high due near the end of October, followed by another 'trainwreck' into the third week of November.

Looking Ahead

- Bond cycles show yields turning higher after another low between now and September 9th.
- Stock cycles show a trend–change high near 9/30, a low near 10/14, and a more major high near 10/30.
- The Bond Market Review wishes you a safe and fun Labor Day weekend! Bring on college football!!!

Treasuries, Agencies, and MBS

As global equities were nose–diving into early last week, yields followed lower as well – with U.S. bonds receiving a flight–to–quality bid. As stocks stabilized, yields snapped back into Thursday (08/27), and have remained in a fairly tight trading range since then. U.S. 10–year yields fell from 2.49% on June 26th down to 2.03% on August 21st. They plunged to 1.91% on Monday the 24th as the Dow dropped nearly 1,100 points in confused trading at the open. When the Dow fought back to lose only 588 points that day, the 10–year sold off back to 2.00%. The Dow gained 1,300 points from its early–Monday trough and, following huge gains on Wednesday and Thursday, actually ended the week 183 points or 1.11% higher – with a relatively small trading range on Friday (08/28). With that recovery, yields rose back to the pre–Fed minute levels from August 18th. That left yields higher by 10.5, 8.5, 14.5, and 19 bps for the week (for the 2, 5, 10, and 30–year sectors). Into today, 2 and 5–year yields were slightly lower for the week, while 10 and 30–year yields rose .5 and 4 bps. MBS spreads (for FNMA 30–year 3.0%) pulled in by 8 bps into August 28th (recovering, after having widened by 3 and 5 bps the 2 weeks before).

There's no scheduled early close for this Friday going into the Labor Day weekend. However, bond–traders have been known to slip away anyway in order to enjoy a last long summer weekend. Last Thursday's (08/27) 7–year note auction was rated above average, following poorer showings for the 2 and 5–year offerings. The Treasury sold $29 billion 7–year notes at 1.93%, with the best demand since November, 2014. Foreign buyers accounted for 50.8% of the supply, compared to 49.1% in July. Next week, the U.S. Treasury will auction $24 billion 3–year notes on Tuesday (09/08), $21 billion 10–year notes on Wednesday, and $13 billion 30–year bonds on Thursday.

8/28/15 Treasury Yield Curve	2-Year: 0.718%	5-Year: 1.513%	10-Year: 2.182%	30-Year: 2.912%
Weekly Yield Change:	+.103	+.085	+.145	+.188%
Support:	0.70/ 0.73/ 0.75/ 0.79%	1.54/ 1.60/ 1.63/ 1.66%	2.20/ 2.23/ 2.29/ 2.32%	2.95/ 3.00/ 3.04/ 3.09%
Targets:	0.67/ 0.65/ 0.62/ 0.59%	1.49/ 1.42/ 1.37/ 1.31%	2.14/ 2.10/ 2.05/ 2.00%	2.87/ 2.83/ 2.77/ 2.72%

Economics

The second estimate (of three) for second–quarter U.S. GDP came in at 3.70%. That was much higher than expected, and attributed to business investment. All the individual components showed more growth than for the first GDP estimate of 2.3%. The Gross Domestic Income rate was only .60%, and should be roughly the same as GDP (as both measure the size and growth of the economy). Averaging the two, which is being used to create a new hybrid series places 2Q growth just below 2.1% – which is of course not quite the good news. Personal Consumption rose 3.10% and the GDP Price Index rose 2.10%. Core PCE rose 1.80%. Nonfarm Productivity jumped 3.30%, while Unit Labor Costs fell 1.40%. IBD/TIPP Economic Optimism fell from 46.9 to 42. University of Michigan Sentiment dropped a point to 91.9, and their Current Conditions component fell 2 points to 105.1. Expectations fell .4 to 83.4. ISM Manufacturing slowed from 52.7 to 51.1 – the slowest pace since May 2013, and Prices Paid fell from 44 to 39. ISM Milwaukee rose from 47.12 to 47.67. Other areas weakened as Chicago Purchasing Managers dropped from 54.7 to 54.4, ISM New York fell from 68.8 to 51.1, Dallas Fed Manufacturing dropped from –4.6 to –15.8, and Kansas City fell from –7 to –9. July Factory Orders rose .40% following a 2.20% June revision (improved by .40%). However, ex Transportation, orders fell .60%.

Initial Jobless Claims fell 6K to 271K, but that's a good drop. Continuing Claims rose 14K to 2,269K. In July, Personal Income rose .40%, while Personal Spending rose .30%. 'Real' Personal Spending rose .20%. The PCE Deflator showed consumption prices rising .10% in July, and only .30% annually. The ex food & energy rate was also .10%, while that annual core pace slowed .10% to 1.20%. Vehicle Sales rose from July's 17.46M pace to 17.72M in August. However domestic sales eased off July's pace with a drop from 13.92M to 13.80M. Pending Home Sales rose .50% in July. The annual pace dropped from 11.10% to 7.20%. MBA Mortgage Applications surged 11.30% – and why not, if one was able to lock in these surprisingly lower rates! July Construction Spending rose .70%. The annual pace rose to 13.9% – the best since March 2006.

Following still–decent ADP numbers which showed private–sector jobs growing by 190K, Thursday will bring jobless claims and Challenger Job Cuts to add two more early reads on August payrolls. Also due are the July Trade Balance (deficit), Bloomberg Consumer Comfort (which rose .9 points to 42), and the service–sector outlook (ISM Non–Manufacturing Composite). Friday gives us the August payroll and unemployment numbers. Next Tuesday (09/08) follows Monday's Labor Day holiday with NFIB Small Business Optimism, the Fed's labor dashboard (Labor Market Conditions Index Change), July Consumer Credit, and JOLTS Job Openings.

Equities

Stocks had an ugly August, but last week ended with quite a recovery from a 'flash crash' type of low. With the Dow off nearly 1,100 points in early Monday trading on August 24th, it was impressive to see it finish up 183.26 points or 1.11% for the week to 16,643.01. It's off 1.75% this week. The S&P gained 17.98 points or .91% to 1,988.87, but is 2.01% lower this week. The Nasdaq had surged 122.29 points or 2.60% to 4,828.33, but is also lower this week – by 1.62% since Friday. The Transports fought back to gain .46% last week, but are .55% lower since Friday. Bank stocks fell .32%, and are one of the weaker groups this week – off 2.94%. Over the past years, we've covered the seasonal tendency for stocks to rise into Labor Day. They're off to a good start.

	Dow:	Nasdaq:	S&P:
Resistance:	16,678/ 16,935/ 17,194/ 17,456	4,807/ 4,879/ 4,949/ 5,019	1,973/ 1,994/ 2,017/ 2,040
Support:	16,168/ 15,978/ 15,786/ 15,658	4,671/ 4,602/ 4,532/ 4,464	1,929/ 1,907/ 1,885/ 1,867

Other Markets

Commodities and Crude Oil checked what looked like a lock for a 9th weekly loss when Crude Oil closed the week with a 2–day surge that followed through to this Monday. That resulted in the largest 3–day gain for Crude since the 1990 Iraqi invasion of Kuwait! It also wiped out a whole month of losses. When we wrote the **BMR** last Wednesday, Crude was 4.57% lower. It ended the week 11.79% higher with back–to–back gains of 10.03% and 5.96%! Monday's 6.24% gain made the 3–day advance 23.87%! It's lost a little ground since, but is still 2.28% higher since Friday. Commodities ended 3.01% higher after being off 3.17% through Wednesday. They're .16% lower after giving up earlier–week gains. The U.S. Dollar gained 1.19%, but is .30% lower this week. The Japanese Yen gained .27%, and then surged 1.13% into today. The Euro lost 1.77%, but is .38% higher since Friday. Corn lost .55%, and is 2.55% lower this week. Cotton fell 5.75%, and is another .89% lower since Friday.

"Wisdom is what's left after we've run out of personal opinions." Cullen Hightower

Additional Information is Available on Request

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