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ECONOMIC TALKING POINTS

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Great Job Numbers! Now the Hard Work REALLY Begins for The Fed.

With today's bullish jobs report for November, the Fed finally got the picture perfect go-ahead for a rate lift-off in two weeks. The zero-bound short-term rate policy, one of the last vestiges of the emergency tools to lift the economy out of the Great Recession, is about to become history. As Janet Yellen said at the Economic Club of Washington earlier this week, "the economy has come a long way toward the FOMC's objective of maximum employment and price stability." The 211,000 jump in November payrolls and the significant upward revisions in September and October just adds more firepower to the argument that the time has indeed arrived to begin normalizing rates.

Chart 1. Unemployment rate, seasonally adjusted, November 2013 – November 2015

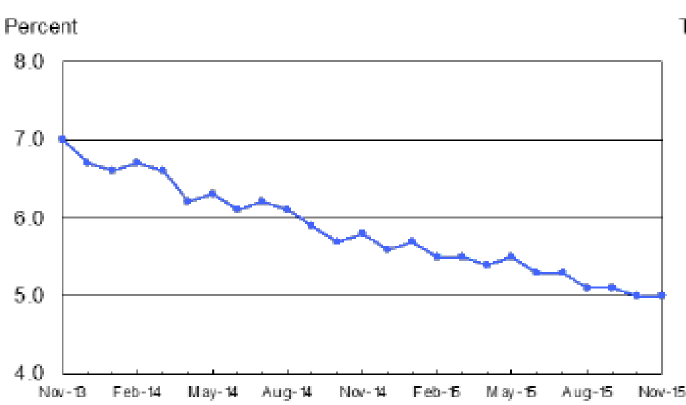
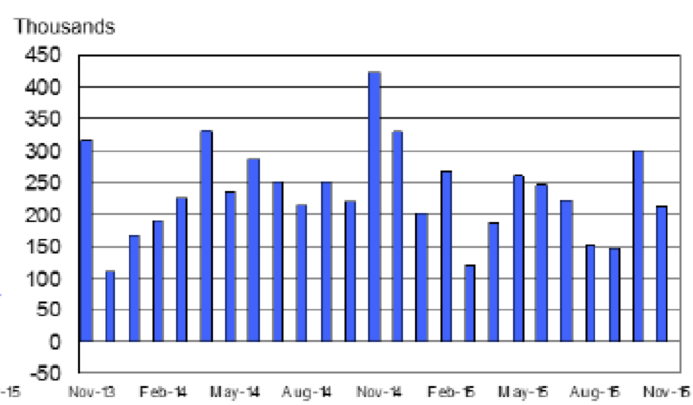


Chart 2. Nonfarm payroll employment over-the-month change, seasonally adjusted, November 2013 – November 2015

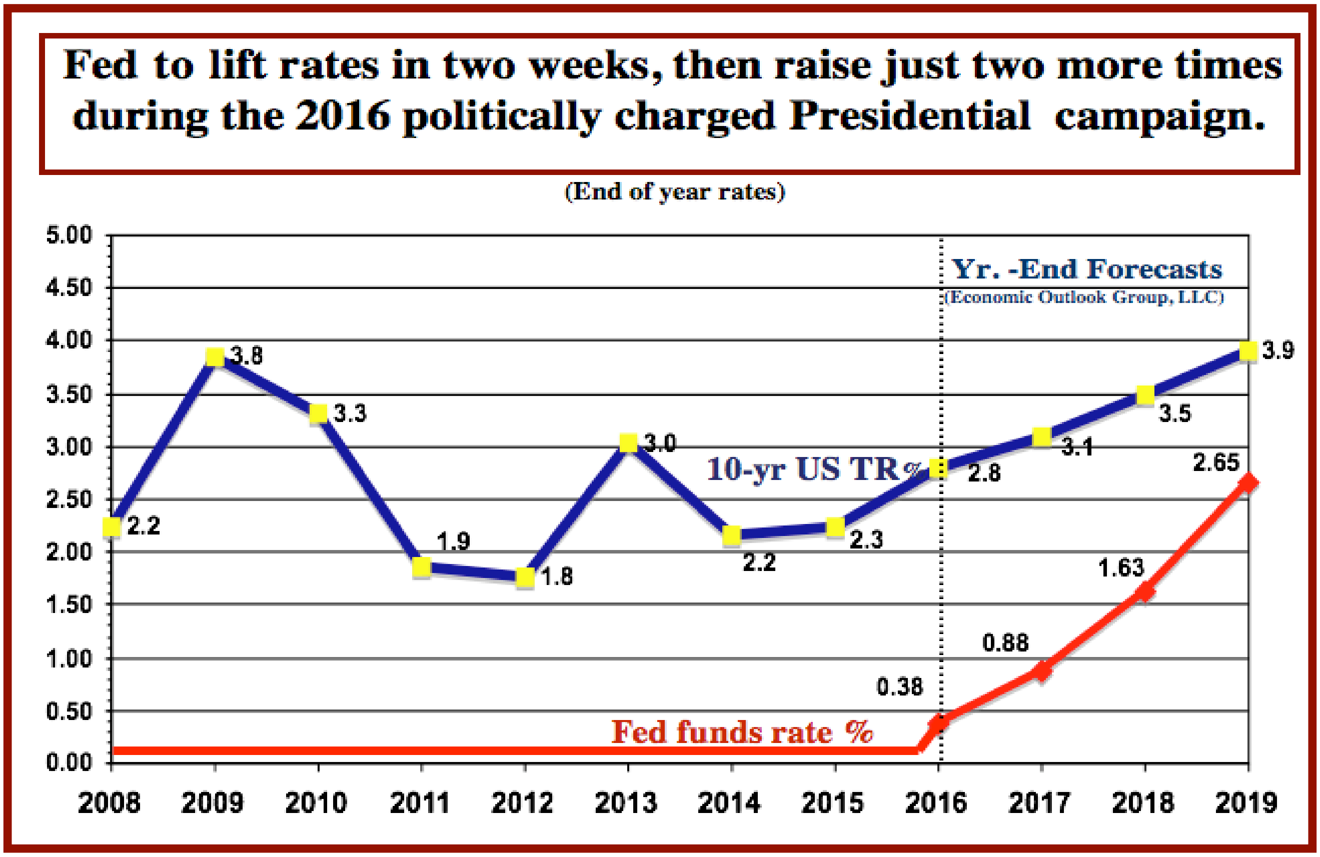


Source: BLS

In a sense, the Fed's work really begins now. Once they raise the target rate by 25 basis points, the focus will immediately shift to how consumers, businesses, lenders, stocks, bonds and currencies will react to this transition in U.S. monetary policy--- and that broad assessment will take time.

We expect the Fed will raise rates no more than two times in 2016, largely because inflation pressures will remain mute --- but also in part because the Fed may choose to keep a low profile during what promises to be highly charged Presidential campaign. Our forecast calls for the effective fed funds rate to reach 0.88% by the end 2016, with the pace of rate increases picking up in 2017 and 2018.

Chart 3. Fed funds to reach 0.88% by end of 2016

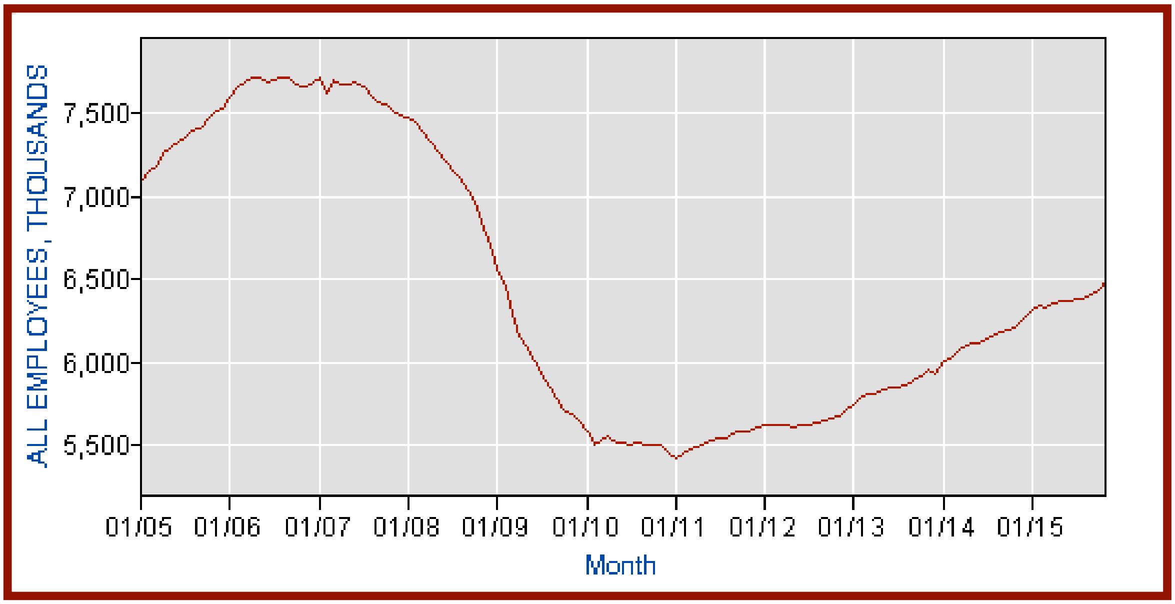


Source: The Economic Outlook Group

Today's job report underscores the fact that while manufacturing activity is contracting, the rest of the domestic economy, which accounts for nearly 90% of GDP, is much more vibrant. There is no better illustration of that than in November's job numbers.

• Construction boosted employment by 46,000 in November, the biggest monthly jump in nearly two years, and lifted total workers in this sector to 6.49 million, the most since January 2009 (Chart 4).

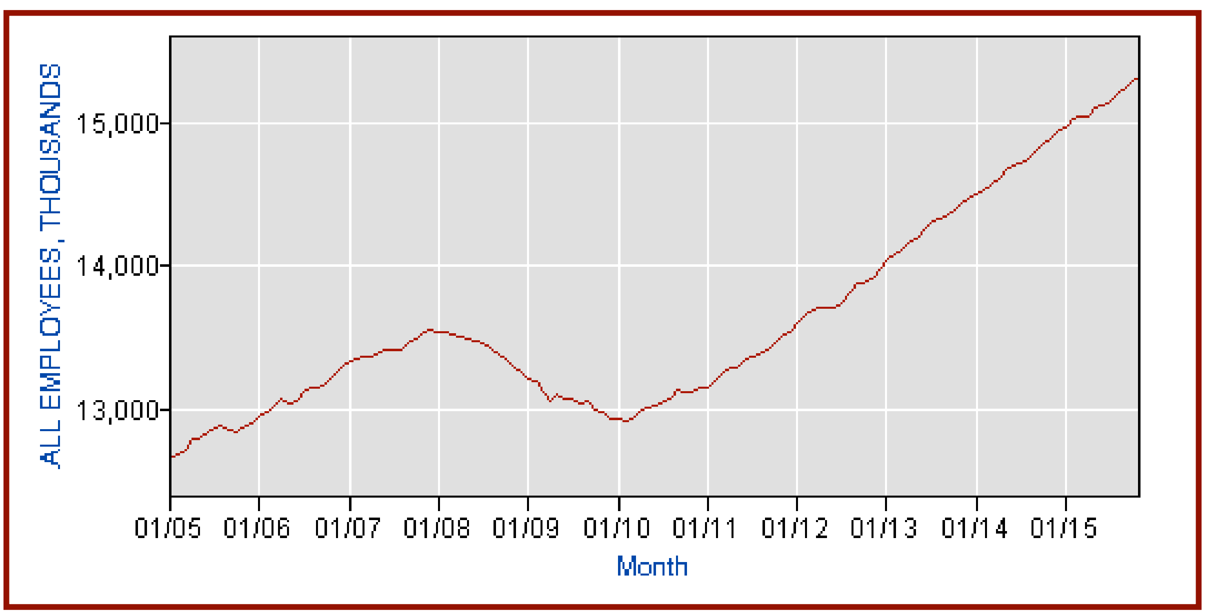
Chart 4. Construction employment



Source: BLS

- **Leisure and hospitality employment accelerated markedly in the second half of this year, with hiring up 39,000 just last month. That brought their total to a record 15.3 million.**

Chart 5. Record employment in leisure and hospitality



Source: BLS

- **Retail added 30,700, lifting jobs here to 15.78 million, an historic high for this industry.**

Drill down further into the report and we see other indicators that suggest employers are growing more confident about the economic outlook.

- For example, temporary hiring has now plateaued as firms become more comfortable adding workers on a permanent basis. The number of temp workers, which typically rises in the early stages of a recovery and then tapers off during the expansion phase, fell 12,300 last month. Only 74,3000 temp workers were hired in the last 12 months, while overall employment climbed more than 2 million in the last 12 months.

- The demand for truckers, which has understandably softened recently given the decline in exports and troubles in the domestic energy sector, rebounded in November, adding 2,300 people. Total employment in the trucking sector now stands at 1.46 million, just shy of it historic high. Its recovery has been helped by the boom in construction activity, auto production and sales, and rising imports.

- Hiring at day care centers also keeps on climbing. Young parents who find employment will make arrangements to drop off their children at these facilities. Since many states require daycare centers to maintain a specific ratio of caregivers to children, the more children brought in, the more adults day care facilities must hire. November's report showed day care centers added another 1,800 people, bringing their total to 880,500, another record for this industry.

Another impressive set of data points can be found in the household survey.

The growth in the labor force averaged 75,000 a month over the past year, yet employment has climbed more than twice that pace, to more than 169,000 a month. And those actively seeking work are having an easier time find it. The median duration of weeks unemployed fell to 10.8 in November, the fewest in seven years.

So, attention now turns the December 15 – 16 FOMC meeting, which is sure to be an historic one not just because we expect to see the rate hike in a decade, but because the Fed will have to come up with fresh language on its forward guidance.

The next FOMC statement will likely hammer the point home that the slope of rate increases will be exceptionally shallow this cycle. The reason for that should be obvious: While the Fed has largely met the goal on achieving full employment, it has fallen short of its second mandate, which is stabilizing inflation at around 2%. That will be a tougher target to meet. With average hourly earnings growing a lackluster between 2% to 2.5% a year, the US dollar holding strong, and with oil prices to remain depressed given today's decision by OPEC to keep production unchanged, there is not much out there to stoke inflation.

Thus, while the call to raise the fed funds rate will be an easy one to make this time, the real challenge is how they will craft their next statement. The goal would be to quash expectations of a rate increase with each subsequent Fed meeting, yet then immediately hedge it by adding the central bank action will always remain --- dare I say it, "data dependant."

Key Economic Forecasts

- Actual
- Forecast

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United States

	I 2014	II 2014	III 2014	IV 2014	I 2015	II 2015	III 2015	IV 2015	I 2016	II 2016	III 2016	IV 2016
Real Gross Domestic Product (GDP):												
%	-0.9	4.6	4.3	2.1	0.6	3.9	2.1	2.7	2.6	3.5	3.2	2.8
Personal Consumption Expenditures:												
PCE	1.3	3.8	3.5	4.3	1.8	3.6	3.0	3.1	2.5	3.6	3.2	3.3
Inflation, end of period, year-over-year:												
CPI %	1.5	2.1	1.7	0.8	-0.1	0.1	0.0	0.6	0.8	1.2	1.5	1.6
Unemployment Rate (end of period):												
%	6.7	6.1	5.9	5.6	5.5	5.3	5.1	4.8	4.9	4.9	5.0	5.2
Non-farm Payrolls, monthly avg. thousand:												
	189	267	237	324	195	231	171	225	235	240	245	250
Treasury 10-yr Note Yield % (end of period)												
	2.72	2.52	2.51	2.17	1.93	2.38	2.06	2.32	2.50	2.65	2.88	3.10
Federal funds rate % (end of period)												
	0.13	0.13	0.13	0.13	0.13	0.13	0.13	0.38	0.38	0.63	0.63	0.88

GDP Growth - Global Economy

Country	2007	2008	2009	2010	2011	2012	2013	2014	2015	2016
US	1.8	-0.3	-2.8	2.5	1.6	2.2	1.5	2.4	2.5	2.8
Eurozone	2.6	0.6	-4.1	1.7	1.4	-0.6	-0.4	0.9	1.3	1.6
United Kingdom	3.1	0.6	-5.2	1.7	0.7	0.3	1.8	3.0	2.4	2.6
Japan	2.1	-0.7	-5.4	4.6	-0.4	1.6	1.5	-0.1	0.5	1.0
Canada	2.7	0.7	-2.8	3.2	2.5	1.7	2.0	2.4	1.0	1.8
India	9.1	8.8	6.3	8.4	8.6	6.7	4.9	7.4	7.3	7.5
China	14.2	9.6	9.2	10.5	9.5	7.8	7.7	7.3	6.7	6.3
Brazil	5.7	5.1	-0.3	7.5	2.7	0.9	2.3	0.1	-3.3	-2.2
Mexico	3.3	1.4	-4.7	5.2	4.0	3.9	1.4	2.1	2.0	2.4
Australia	4.0	2.3	1.2	2.8	2.6	3.6	2.4	2.7	2.1	2.3
Russia	8.1	5.6	-7.9	4.0	4.3	3.4	1.3	0.6	-3.6	-1.0
World	5.4	1.6	-1.9	4.2	3.0	2.6	2.9	3.0	2.7	3.1

Key Currency Values

	End 2008	End 2009	End 2010	End 2011	End 2012	End 2013	End 2014	End 2015	End 2016
USD/Yen	91	93	81	77	87	105	119	125	133
Euro/USD	1.40	1.43	1.34	1.29	1.32	1.37	1.21	1.08	1.10

Oil (Brent spot) & Gasoline (Average retail unleaded, $)

	End 2008	End 2009	End 2010	End 2011	End 2012	End 2013	End 2014	End 2015	End 2016
Crude oil per barrel	46	78	95	107	111	111	58	45	59
Gasoline	1.61	2.57	3.00	3.27	3.30	3.32	2.26	2.03	2.30

Major Stock Indexes

	End 2012	End 2013	End 2014	% Change '14	End 2015	% Change '15
DJIA	13,104	16,577	17,823	7.5	18,600	4.4
S&P 500	1,426	1,848	2,059	11.4	2,110	2.5
NASDAQ	3,019	4,177	4,736	13.4	5,157	9.1
RUSSELL 2000	849	1,164	1,205	3.5	1,277	6.0