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Fed Changes Tune On Interest Rates

Weekly Update – May 23, 2016

Stocks closed out a bumpy week mixed, ending a three-week stretch of losses for the S&P 500 and NASDAQ. The Dow, however, extended losses for a fourth straight week for the first time since 2014.ⁱ For the week, the S&P 500 gained 0.28%, the Dow lost 0.20%, the NASDAQ gained 1.10%, and the MSCI EAFE added 0.16%.ⁱⁱ

Market reactions to the release of the April Federal Reserve Open Market Committee meeting minutes drove much of last week's volatility. The official minutes showed that the Fed is moving away from its cautious stance and is open to raising interest rates as soon as June if data points to a solid second quarter.ⁱⁱⁱ The unexpected hawkishness surprised many investors who weren't expecting a hike until later this year.

However, some professional economists predicted a June hike. The most recent Wall Street Journal survey of economists showed that their experts were split, with 31.4% predicting a June increase, 21.4% favoring a July hike, and 31.4% forecasting a September increase.^{iv} On the other hand, Wall Street largely discounted a June move. Early in the week, before the minutes were released, traders predicted just a 4% chance of a June rate hike. By Friday, that probability had increased to 30%.^v Clearly, the new information is forcing investors to revise their expectations for interest rate movements this year.

The labor market will play a major role in the Fed's June decision. The April jobs report was softer than expected, showing that many employers were reluctant to hire in the face of uncertain business conditions.^{vi} The May jobs report, due on June 3rd, will be key to showing whether the labor market has returned to a strong trend or is continuing to weaken.

Will a strong May jobs report guarantee a June rate hike? Some experts think so while others think the risks posed by Britain's upcoming vote on whether to leave the EU (the "Brexit" you may have read about) will be enough to give the Fed pause.^{vii} All told, it's likely to be a lively June meeting at the Fed.

Volatility is likely to continue in the days and weeks ahead as analysts fixate on predicting when the central bank will raise rates again. While short-term volatility can be stressful to investors who would prefer a steady ride, it's important not to let intraday swings and bumps in the road derail your long-term investment strategies. We'll keep you updated.

ECONOMIC CALENDAR:

Monday: PMI Manufacturing Index Flash

Tuesday: New Home Sales

Wednesday: International Trade in Goods, EIA Petroleum Status Report

Thursday: Durable Goods Orders, Jobless Claims, Pending Home Sales Index

Friday: GDP, Consumer Sentiment, **Janet Yellen Speaks 10:30 AM ET**

Data as of 5/20/2016	1-Week	Since 1/1/16	1-Year	5-Year	10-Year
Standard & Poor's 500	0.28%	0.41%	-3.46%	10.79%	6.20%
DOW	-0.20%	0.44%	-4.29%	7.97%	5.70%
NASDAQ	1.10%	-4.75%	-5.96%	14.03%	11.74%
U.S. Corporate Bond Index	-0.81%	4.74%	4.27%	5.24%	7.52%
International	0.16%	-4.78%	-15.69%	-0.82%	-1.15%
Data as of 5/20/2016	1 mo.	6 mo.	1 yr.	5 yr.	10 yr.
Treasury Yields (CMT)	0.26%	0.46%	0.67%	1.38%	1.85%

Notes: All index returns exclude reinvested dividends, and the 5-year and 10-year returns are annualized. Sources: Yahoo! Finance, S&P Dow Jones Indices, and Treasury.gov. International performance is represented by the MSCI EAFE Index. Corporate bond performance is represented by the SPUSCIG. Past performance is no guarantee of future results. Indices are unmanaged and cannot be invested into directly.

HEADLINES:

April housing starts surge. Groundbreaking on single- and multi-family homes jumped 6.6% last month as construction firms grew more optimistic about business prospects.^{viii}

Industrial production rises. Stronger demand for utilities drove industrial production 0.7% higher in April. However, the manufacturing component rose just 0.3% after declining in March, indicating that U.S. manufacturers are still struggling.^{ix}

Jobless claims fall from 14-month high. Weekly claims for new unemployment benefits fell last week, showing that the previous weeks of increases might have been an anomaly.^x

Existing home sales increase more than expected. Sales of existing homes rose 1.7% in April and March's resales were revised slightly higher, suggesting that the housing market is gaining ground.^{xi}

QUOTE OF THE WEEK



"Keep working no matter what happens. If things are good, keep working. If things are bad, keep working."

– Moby

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Investing involves risk including the potential loss of principal. No investment strategy can guarantee a profit or protect against loss in periods of declining values.

Diversification does not guarantee profit nor is it guaranteed to protect assets.

The Standard & Poor's 500 (S&P 500) is an unmanaged group of securities considered to be representative of the stock market in general.

The Dow Jones Industrial Average is a price-weighted average of 30 significant stocks traded on the New York Stock Exchange and the NASDAQ. The DJIA was invented by Charles Dow back in 1896.

The Nasdaq Composite is an index of the common stocks and similar securities listed on the NASDAQ stock market and is considered a broad indicator of the performance of stocks of technology companies and growth companies.

The MSCI EAFE Index was created by Morgan Stanley Capital International (MSCI) that serves as a benchmark of the performance in major international equity markets as represented by 21 major MSCI indexes from Europe, Australia and Southeast Asia.

The Dow Jones Corporate Bond Index is a 96-bond index designed to represent the market performance, on a total-return basis, of investment-grade bonds issued by leading U.S. companies. Bonds are equally weighted by maturity cell, industry sector, and the overall index.

The S&P/Case-Shiller Home Price Indices are the leading measures of U.S. residential real estate prices, tracking changes in the value of residential real estate. The index is made up of measures of real estate prices in 20 cities and weighted to produce the index.

The 10-year Treasury Note represents debt owed by the United States Treasury to the public. Since the U.S. Government is seen as a risk-free borrower, investors use the 10-year Treasury Note as a benchmark for the long-term bond market.

Opinions expressed are subject to change without notice and are not intended as investment advice or to predict future performance.

Past performance does not guarantee future results.

You cannot invest directly in an index.

Consult your financial professional before making any investment decision.

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ⁱ <http://www.cnbc.com/2016/05/20/us-markets.html>

ⁱⁱ <http://finance.yahoo.com/q/hp?s=%5EGSPC&a=04&b=16&c=2016&d=04&e=20&f=2016&g=d>

<http://finance.yahoo.com/q/hp?a=04&b=16&c=2016&d=04&e=20&f=2016&g=d&s=%5EDJI%2C+&q=1>

<http://finance.yahoo.com/q/hp?a=04&b=16&c=2016&d=04&e=20&f=2016&g=d&s=%5EIXIC%2C+&ql=1>

<https://www.msci.com/end-of-day-data-search>

ⁱⁱⁱ <http://www.cnbc.com/2016/05/18/federal-reserve-minutes.html>

^{iv} <http://projects.wsj.com/econforecast/#qa=20160501001&e=1462995269111>

^v <http://www.reuters.com/article/usa-stocks-weekahead-idUSL2N18H1MK>

^{vi} <https://www.zacks.com/stock/news/217943/will-the-fed-raise-rates-in-june-outlook-uncertain>

^{vii} <https://www.zacks.com/stock/news/217943/will-the-fed-raise-rates-in-june-outlook-uncertain>

^{viii} <http://www.foxbusiness.com/markets/2016/05/17/april-housing-starts-jump-6-6.html>

^{ix} <http://www.federalreserve.gov/releases/g17/current/>

^x <http://www.foxbusiness.com/markets/2016/05/19/weekly-jobless-claims-fall-by-16000.html>

^{xi} <http://www.foxbusiness.com/markets/2016/05/20/april-existing-home-sales-rise-more-than-expected.html>