

October 2017

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- According to the advance estimate of the Bureau of Economic Analysis, real GDP increased by 3.0% quarter-over-quarter (qoq) in Q3.
- National industrial production returned to growth in September.
- Consumer confidence softened after several months of strengthening.
- Despite continued growth in both manufacturing and service sectors, Texas economy in general saw mixed developments in September.
- Unlike employment, the situation with the number of unemployed notably improved in September at both national and Texas level.
- In September, consumer prices continued to grow at virtually the same pace as in August.
- The situation with the housing market improved at the national level but further deteriorated in Texas in September.

Executive Summary

In Q3, the economy grew at the same pace as in the previous quarter. Advanced estimate of the Bureau of Economic Analysis showed that national GDP expanded by 3.0% qoq on the back of increases in nonresidential fixed investment, personal consumption expenditures, private inventory investment, exports, and federal government spending.

The US industrial production reversed the trend again. It returned to growth in September after a decline in August. All the major industrial production components returned to growth with the fastest one registered in utilities. Manufacturing inched up thanks to growth in durables which more than offset the decline in nondurables.

Consumer confidence softened for the first time in a while at the national level. This was the result of less optimistic perceptions of the current business conditions. In particular, there was an increase in the number of respondents claiming business conditions are “bad” and a decline in the number of those saying business conditions are “good”. At the same time, the short-term expectations remained on the upwards trend.

The Texas economy sustained mixed developments in September. Texas manufacturing activity continued to expand but the growth pace notable decelerated. Service sector also posted growth despite some deterioration in labor market indicators and perceptions of broader business conditions. Consumer confidence softened after one month of solid strengthening.

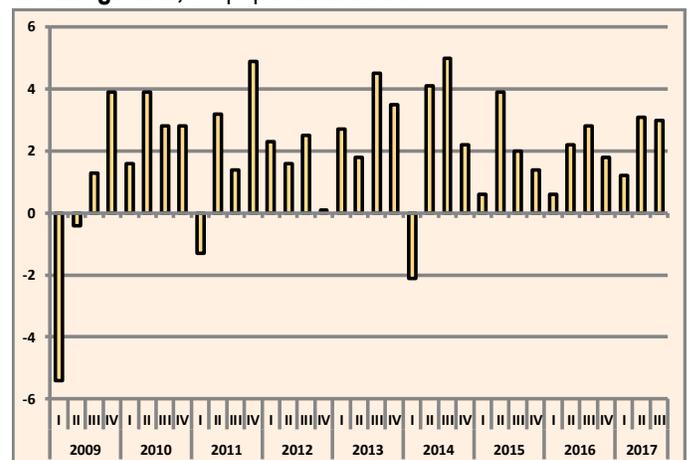
Both national and Texas labor markets saw little changes in September. Employment remained almost flat both in Texas and at the national level. On the other hand, unemployment declined also in Texas and in the US in general. At the same time, changes at the national level were more notable.

There were no changes in the policy rate in September, same as in the monetary policy stance. Consumer prices grew a bit faster than in August being pushed upwards by more significant increase in energy prices. Housing market situation improved at the national level but deteriorated in Texas.

Economic Growth

Economic growth remained virtually unchanged in Q3 as compared to Q2. The Bureau of Economic Analysis has published its advance estimate of real GDP growth. According to the estimate, real GDP increased by 3.0% qoq in Q3. GDP growth was driven by expansion of personal consumption expenditures (2.4% qoq), private inventory investment, nonresidential fixed investment (3.9% qoq), exports (2.3% qoq), and federal government spending (1.1% qoq). Decline of imports (by 0.8%

1. GDP growth, % qoq at annual rates



Source: The U.S. Bureau of Economic Analysis

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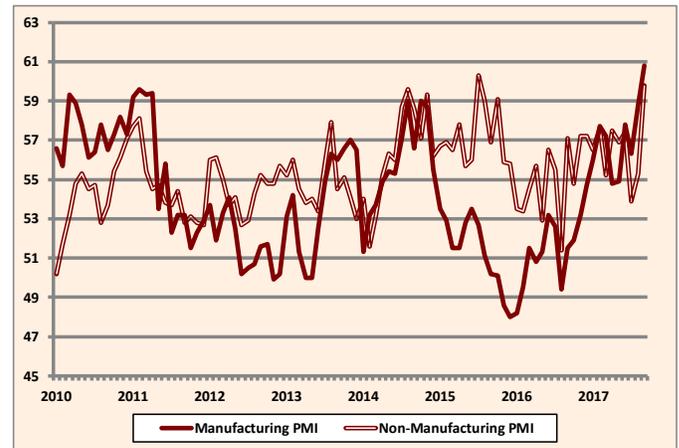
qoq) also made positive contributions to GDP growth as it is subtracted in the GDP calculation. The mentioned increases were partially offset by negative contributions from residential fixed investment (-6.0% qoq) and state and local government spending (-0.9% qoq).

National industrial production returned to growth in September. After a one-month decline in August, industrial production edged up by 0.3% mom. All its major components returned to growth but the largest increase was observed in utilities at 1.5% mom. Mining expanded by 0.4% mom on the back of oil and gas extraction. Growth in oil and gas extraction more than compensated for declines in other mining components. Manufacturing inched up by 0.1% mom as a 1.0% mom increase in durables outweighed a 0.9% mom decrease in nondurables. Nonmetallic mineral products, machinery, and electrical equipment, appliances, and components were the drivers of growth in durables growing by around 3% mom each. Most of the nondurables posted declines with the largest one recorded for chemicals. The over-year growth of industrial production advanced to 1.6% being pushed upwards by increases in manufacturing (1.0% yoy) and mining (9.8% yoy), while utilities still declined (by 4.1% yoy).

National manufacturing expanded for 13th consecutive month in September. All the PMI components except for Inventories and imports posted increases pushing the PMI upwards by 2.0 percentage points to 60.8%. Only customers' inventories index remained below 50% (42.0%) meaning that it continued to decline. Such important indexes as new orders, production, and employment were above 60% meaning that we are almost certain the sector in general will continue growing in October. Only furniture and related products reported decline in August, while all the other manufacturing industries reported increases.

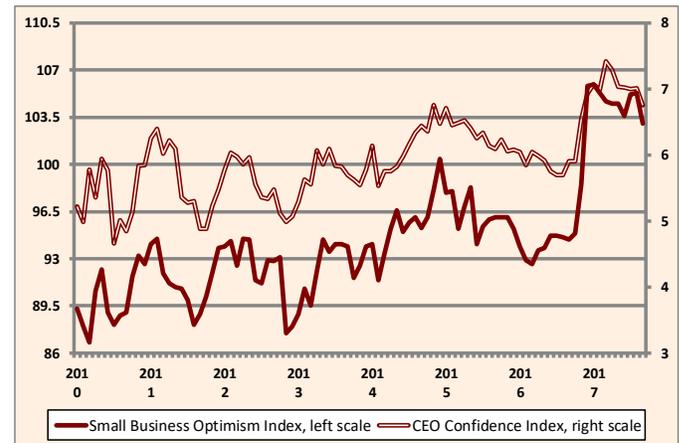
The non-manufacturing sector grew even faster in August marking the 93rd consecutive monthly growth. The NMI index expanded by 4.5 percentage points to 58.3%. This growth was ensured by increases in all the NMI components except for inventories. Nevertheless, even inventories with its lowest reading among the other NMI components at 51.5% continued to grow as it stayed above 50% threshold, though at slower pace. The vast majority of non-manufacturing industries,

2. PMI, indexes



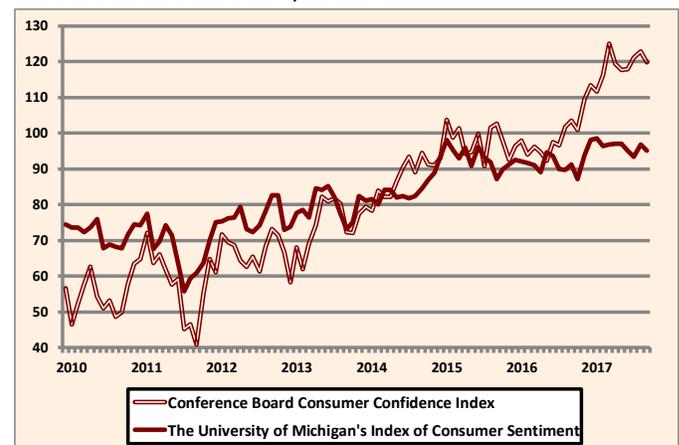
Source: Institute for Supply Management

3. Business confidence, indexes



Source: Chief Executive, National Federation of Independent Business

4. Consumer confidence, indexes



Source: Conference Board, The University of Michigan

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namely 15, reported growth, while only two industries reported declines. Those were arts, entertainment and recreation and mining.

After several months of strengthening, consumer confidence slightly softened in August. The Conference Board Consumer Confidence Index dropped to 119.8 due to deteriorated perceptions of the present situation. In particular, the Present Situation Index dropped from 148.4 to 146.1. At the same time, the Expectations Index once again marginally improved to 102.2. Overall consumers' appraisal of current conditions deteriorated as the number of those saying business conditions are "bad" increased and the number of those saying business conditions are "good" declined a bit. The situation with appraisal of current labor conditions did not differ much. The short-term expectations, though, further improved in terms of both business conditions and labor market.

The Texas economy saw mixed developments in September. Manufacturing activity continued to expand although its growth decelerated once again. The production index edged down further to 19.5 meaning that output grew at almost the same pace as a month ago. Other measures of current manufacturing activity indicated continued growth but at a bit slower pace. At the same time, perceptions of broader business conditions and labor market measures further improved. Similarly, expectations regarding future business conditions also improved.

After some deceleration in August, growth of Texas service sector picked up slightly in September. The revenue index increased from 14.2 to 15.9. At the same time, both labor market indicators and perceptions of broader economic conditions were slightly less optimistic in the reporting month. Expectations regarding future business conditions further improved.

Consumer confidence softened again in September after one month of significant strengthening. Furthermore, it softened beyond the level observed in July. The Conference Board Consumer Confidence Index dropped 145.4 to 126.5. Thus, Texas consumer confidence level became closer to the country level in the reporting month.

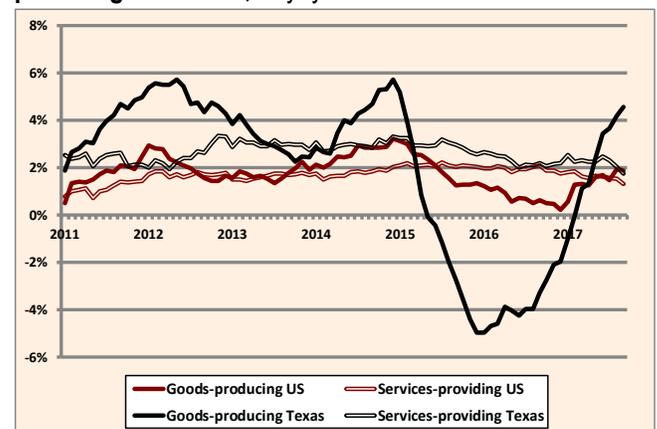
Texas exports decreased by 3.3% mom in August. At the same time, the over-year growth of exports remained at relatively high rate of 8.6%, especially comparing to the national level of 3.9%.

Employment

The national labor market conditions slightly improved in September. Unlike in several previous months, the employment changed little, while unemployment notable declined. Total nonfarm payroll employment edged up by 38,000 which is less than 0.1% mom. The largest employment gains were reported by transportation and warehousing (18,300 or 0.4% mom). Food services and drinking places dropped sharply (63,700 or 0.5% mom). Decreases in employment of financial activities and professional and business services were much smaller (53,000 or 0.6% mom and 51,000 or 0.2% mom respectively).

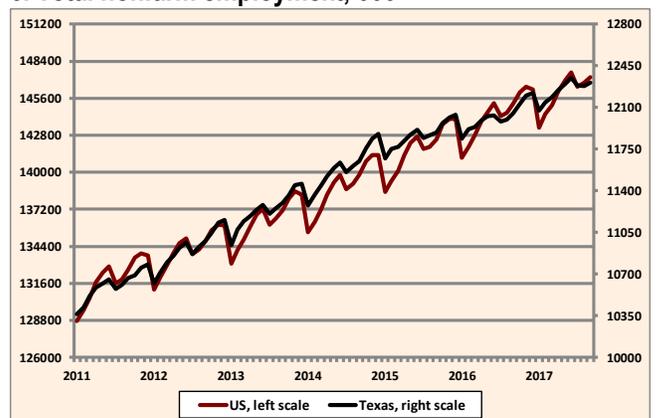
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5. Jobs growth in private goods-producing and service providing industries, % yoy



Source: Bureau of Labor Statistics

6. Total nonfarm employment, 000



Source: Bureau of Labor Statistics

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Other major industries reported little or no changes in employment. Compared to September 2016, total nonfarm payroll employment increased by 1.87 million or 1.3%. The number of unemployed decreased by 331,000 to 6.8 million which led to a 0.2 percentage point drop in the unemployment rate to 4.2%.

Texas labor market conditions saw little changes for the second month in a row. Total nonfarm employment dropped 5,000 jobs (less than 0.1% mom). Five industries generated more than 4,000 new jobs, including mining and construction. However, there also were industries with high employment declines which more than offset the mentioned gains. Leisure and hospitality lost 19,600 jobs or 1.5% mom, while health care and social assistance observed a 7,500 job drop (0.5% mom). Over year, total nonfarm employment expanded by 258,500 or 2.1%. The situation with unemployment improved again in September. The number of unemployed decreased by 15,871 (2.8% mom). The unemployment rate lowered to 4.0%.

Monetary Policy and Asset Prices

At its October meeting, the Federal Open Market Committee decided to maintain the target range for the federal funds rate at 1.0-1.25% level. The monetary policy stance also sustained no changes and remained accommodative.

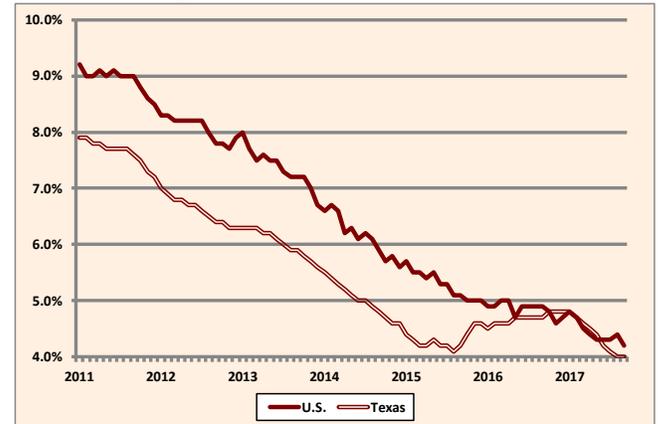
Growth of consumer prices insignificantly accelerated in September. The 0.5% mom growth of the all items index was the result of much faster growth of energy prices compared to August. The pace of energy prices growth more than doubled to 6.1% mom in the reporting month. This growth was driven by accelerated increase in prices of energy commodities (gasoline prices grew by 13.1% mom, while prices of fuel oil expanded by 8.2% mom). At the same time, food prices and prices of all items less food and energy remained virtually flat. In over-year terms, energy prices were also the major driver of consumer inflation. Acceleration of growth in the energy index to 10.1% yoy pushed price growth of the all items upwards to 2.2% yoy. Food prices and prices of all items less food and energy saw little changes in dynamics in September, as they grew by 1.2% yoy and 1.7% yoy respectively.

The housing market saw some improvements at the

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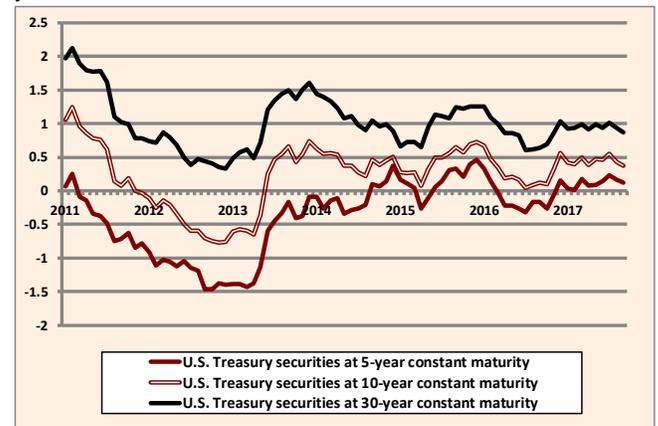
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7. Jobless rate, %



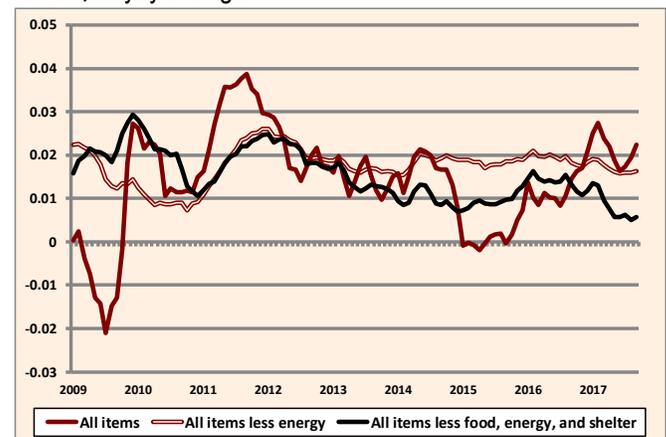
Source: Bureau of Labor Statistics

8. Borrowing rates (quoted on investment basis), % per year inflation indexed



Source: Federal Reserve System

9. CPI, % yoy change



Source: Bureau of Labor Statistics

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national level and negative developments in Texas in September. The national existing-home sales reversed the trend in September after three straight months of decline. Total existing-home sales edged up by 0.7% mom to a seasonally adjusted annual rate of 5.39 million. At the same time, the year-over-year growth remained negative at 1.5% and is the second slowest behind only that observed in August. Low supply and fast growth of prices were the main reasons of lower than expected growth in sales over the last several months. The median existing-home price posted another over-year growth, this time of 4.2% to USD 245,100. That was the 67th straight month of year-over-year gains in prices. Total housing inventory grew by 1.6% mom to 1.9 million existing homes available for sale which is still 6.4% lower than a year ago. Unsold inventory remained flat at 4.2-month supply at the current sales pace. Texas actual existing-home sales declined for the third month in a row. They dropped 8.5% mom to 28,450 but remained almost flat in over-year terms. The median existing-home price continued to expand at quite fast rate of 6.2% yoy reaching USD 223,000. The unsold inventory declined for the first time in nine months. They inched down to 3.9-month supply at the current sales pace.

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