ECONOMIC OUTLOOK
AS OF JUNE 30, 2015

ECONOMIC OUTLOOK

GENERAL ECONOMIC CONDITIONS

The GDP report found that the U.S. economy expanded at a faster pace in the second quarter, falling in line with economists' predictions and the Federal Reserve's view that the economy continues to improve incrementally. Further, the first-quarter GDP rate was revised upward, eliminating the previously reported contraction. Consumer spending grew more than was expected in the second quarter and continued to push the economy forward. Much of the improvement in consumer spending was attributed to increased employment rather than higher incomes, as household earnings have yet to see any significant boost. As a result, the increased spending came from decreased savings, as the saving rate fell nearly half a percentage point. As noted by the Federal Reserve in its June statement, business spending remained weak, with business investment falling at a 0.6% rate in the second quarter, the worst performance since the third quarter of 2012. Government outlays were another source of weakness in the second quarter, rising minimally after shrinking in the first quarter. Increased spending among state local agencies was nearly wiped out by a drop in spending at the federal level. Net exports, which had dragged GDP down in the prior two quarters, had little influence on the second-quarter growth.

The Conference Board reported that the Leading Economic Index continued to rise in June and that the strengths among the leading indicators remained more widespread than the weaknesses. The report stated that the recent increases in the Leading Economic Index indicate continued strength in the economic outlook for the remainder of 2015.

Consumer optimism rose in June, as both the Conference Board's Consumer Confidence Index and Thomson Reuters/University of Michigan's Consumer Sentiment Index improved. The Conference Board report found that the increased optimism came from consumers' improved perceptions of current business and employment conditions. The report from the Thomson Reuters/University of Michigan found that the first half of 2015 has been the largest and most sustained increase in economic optimism since 2004. The report included the caveat that, because the gains in the Consumer Sentiment Index were so outsized, some of the improvement may be the result of survey respondents having a new acceptance of lesser economic standards.

Measures of business owners' optimism declined in June. The National Federation of Independent Business reported that its Small Business Optimism Index retreated, driven down by owners' decisions to scale back their spending plans and their more pessimistic expectations for revenue and business conditions. The Wells Fargo/Gallup Small Business Index also lost ground, with the metric that measures how business owners regard their current revenue causing the majority of the downturn.

Job growth continued in June, and the unemployment rate declined to its lowest level since April 2008. A shrinking labor force contributed somewhat to the decline, as indicated by a drop in the labor-force participation rate. As of June, the private sector has added 12.8 million jobs over 64 straight months of job growth, extending the longest streak on record.

Both the manufacturing sector and services sector continued to expand in June, as measured by the Institute of Supply Management's respective indexes. The pace of expansion in both the manufacturing sector and services sector quickened in June. Further, both indexes remained at readings indicating that the U.S. economy continues to expand.

Industrial production expanded in June for the first time in three months. While manufacturing was unchanged, both the output of utilities and mining rose.

The Federal Reserve maintained its decision to leave the target for the federal funds rate unchanged in the second quarter. It did, however, state that it would continue to assess labor market conditions and inflation expectations to determine whether raising the rate would be appropriate in the future. The Federal Reserve also continued its existing policy of reinvesting principal payments from its holdings of agency debt and agency mortgage-backed securities.

The blue chip stocks comprising the Dow Jones Industrial Average gave up some ground in the second quarter. T. Rowe Price found that relief over corporate earnings growth and enthusiasm about a reaccelerating U.S. economy were dragged down by worries over the ongoing Greek debt crisis. The Nasdaq, boosted by merger and acquisition activity, managed to break the record high it established in 2000, before pulling back a bit at the end of the quarter. The smaller-cap indexes experienced mixed performance in the second quarter, with small-cap stocks outperforming the large-cap stocks, while midcaps performed the worst among the major benchmarks. Stock market volatility remained mostly mild, as measured by VIX. U.S. Treasuries posted their first quarterly loss since 2013, as fears of an imminent Federal Reserve rate increase outweighed demand for safe-haven assets as Greece moved toward default.

The Consumer Price Index rose each month in the second quarter. The recent rise was driven by higher energy costs, particularly the gas index, which rose 10.4% in May and 3.4% in June. The Producer Price Index rose in both May and June but is down 0.7% over the past 12 months. The June rise in the Producer Price Index was attributed primarily to increased energy costs, with the gas index leading the advance.

The housing market indicators were strongly positive in June. Housing starts and building permits rose in June and well exceeded their levels from a year ago. The National Association of Home Builders/Wells Fargo Housing Market Index increased notably, with the components that measure current and future sales expectations hitting their highest levels since the fourth quarter of 2005. Existing-home sales rose in June to their highest pace in over eight years, and homes sold the quickest since the National Association of Realtors began tracking sale times in 2011. Home values increased from their year-ago levels to exceed the peak median sales price set in July 2006. The Realtors Confidence Index for the current conditions of single-family homes was unchanged but remained at a reading indicating most respondents viewed the market as "strong." The National Association of Realtors Pending Home Sales Index retreated slightly in June but sat just below a greater-than-nine-year high.

GROSS DOMESTIC PRODUCT

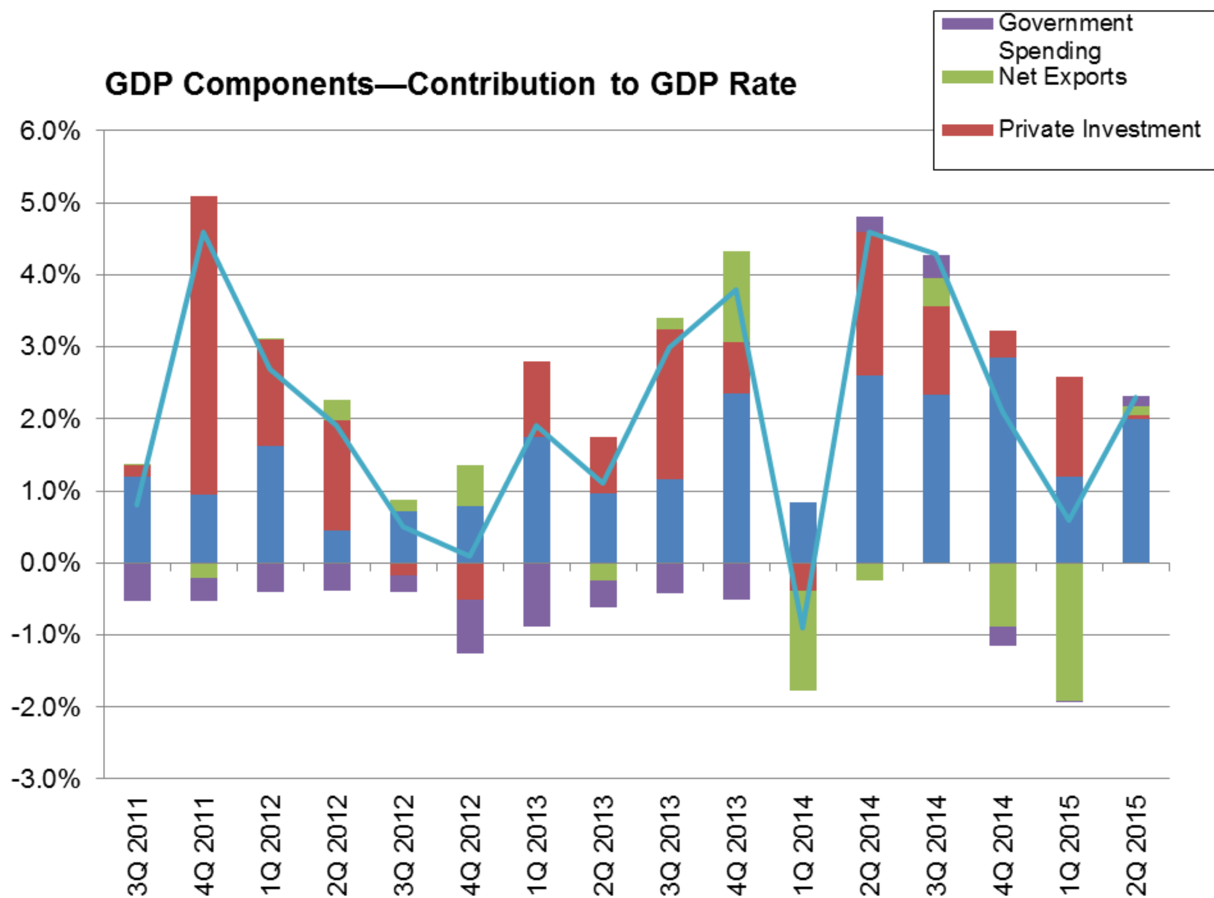
The Bureau of Economic Analysis reported that the nation's economy—as indicated by GDP—grew at an annual rate of 2.3% in the second quarter of 2015. This was consistent with forecasts, as a survey conducted by Bloomberg found that the median forecast of economists was a 2.5% rate. This was a sharp acceleration from the moderate growth of the first quarter, when GDP grew at a 0.6% rate. The first-quarter GDP rate was only positive after a recent revision, as the

previously reported rate indicated that the U.S. economy contracted in the first quarter. GDP is the total market value of goods and services produced in the U.S. economy and is generally considered the most comprehensive measure of economic growth. In 2014, the economy grew 2.4% from the year before, the biggest advance since 2010, following a 1.5% expansion in 2013.

Final sales of domestic product rose in the second quarter, increasing at a rate of 2.4%. This was in contrast to declining at a rate of 0.2% in the first quarter. Final sales are GDP minus the influence of private inventory investment, which tends to be volatile from quarter to quarter. The Economic Policy Institute has stated that final sales are arguably a better indicator of underlying economic strength than GDP.

The increase in GDP in the second quarter was the result of positive contributions from consumer spending, exports, state and local government spending, and residential fixed investment. The second-quarter GDP increase was offset by negative contributions from federal government spending, private inventory investment, and nonresidential fixed investment. Imports, which are a subtraction in the calculation of GDP, increased.

The acceleration in real GDP growth in the second quarter reflected an upturn in exports, an acceleration in consumer spending, a deceleration in imports, and an upturn in state and local government spending. This acceleration was partly offset by downturns in private inventory investment, in nonresidential fixed investment, and in federal government spending, and a deceleration in residential fixed investment.



CONSUMER SPENDING

Consumer spending grew at a rate of 2.9% during the second quarter of 2015, an acceleration from the first quarter's pace of 1.8%. Consumer spending—also referred to as “personal consumption”—accounts for approximately 70% of the U.S. GDP.

The second quarter’s growth in consumer spending contributed 1.99 percentage points to the second-quarter GDP, more than its 1.99-percentage-point contribution in the first quarter.

Overall consumer spending increased 2.7% in 2014, after growing 1.7% in 2013.

Consumer spending on durable goods—items meant to last three years or more, such as computers, cars, and machinery—rose in the second quarter at a rate of 7.3%. This was a notable acceleration from the 2.0% rate in the first quarter. Consumer spending on durable goods rose 5.9% in 2014 after increasing 5.8% in 2013.

Consumer spending on nondurable goods—items such as food and gasoline—increased at a rate of 3.6% in the second quarter, compared with rate of 0.7% in the first quarter. Consumer spending on nondurable goods increased 2.1% in 2014 and 1.9% in 2013.

Service expenditures grew at a rate of 2.1% in the second quarter of 2015, matching its rate from the prior quarter. Consumer spending on services increased 2.4% in 2014 and 1.0% in 2013.

While American spending increased overall in the second quarter, it unexpectedly dipped in June, breaking four consecutive months of increased outlays. U.S. retail sales retreated 0.3% in June, far below the expected gain of 0.3% in a Bloomberg survey of economists. Estimates in the Bloomberg survey ranged from a decline of 0.2% to a gain of 0.8%, so the actual June retail sales figure was below even that of the most pessimistic forecast. Regardless, retail sales were still up 1.4% from one year ago.

The declines were broad-based in June, with eight of the 13 major retail categories seeing weaker sales. Furniture and home stores (-1.6%), clothing stores (-1.3%), home improvement stores (-1.3%), and auto dealers (-1.1%) saw the largest drop in sales. The largest advances came from electronic stores (+1.0%), gas stations (+0.8%), and general merchandise stores (+0.7%).

Core retail sales slipped 0.1% in June but were up 2.1% from one year ago. The core retail sales figure excludes sales of automobiles, gasoline, building materials, and food services and corresponds most closely with the consumer-spending component of gross domestic product.

Figures from Ward’s Automotive Group revealed that cars and light trucks sold at a 17.1 million annualized rate in June, down from a 17.7 million pace in May. Still, June capped the strongest quarter of auto sales since 2005. So far, in 2015, auto sales have averaged a 16.8 million rate, beating last year’s 16.4 million rate, which was the strongest in eight years.

GOVERNMENT SPENDING

Total government spending rose at a rate of 0.8% in the second quarter of 2015, breaking two consecutive quarterly declines. This quarter’s advance in government spending added 0.14 percentage point to the second-quarter GDP rate. Total government spending fell 0.6% in 2014 and 2.9% in 2013.

Federal government spending fell at a rate of 1.1% in the second quarter, the eighth decline in the past 11 quarters. Federal government spending subtracted 0.08 percentage point from the second-quarter GDP rate. Spending by the federal government declined 2.4% in 2014 and 5.7% in 2013.

National defense spending retreated 1.5% in the second quarter of 2015. This was in contrast to an increasing rate of 1.0% in the prior quarter. Defense spending has fallen in nine of the past 11 quarters. Defense spending declined 3.8% in 2014 and 6.7% in 2013.

Federal nondefense spending declined at a rate of 0.5% in the second quarter, its first retreat in the past four quarters. Federal nondefense spending dropped 0.1% in 2014 after falling 4.0% in 2013.

State and local government spending increased at a rate of 2.0% in the second quarter of 2015, its fourth advance in the last five quarters. The retreat in state and local government spending made a 0.21-percentage-point contribution to the second-quarter GDP rate. State and local government spending rose 0.6% in 2014 after falling 1.0% in 2013.

FIXED INVESTMENT

Business investment, also referred to as “nonresidential fixed investment,” fell at a rate of 0.6% in the second quarter of 2015. This was the first retreat in business investment in 11 quarters. The drop in business investment subtracted 0.07 percentage point from the second-quarter GDP. Business spending grew 6.2% in 2014 after increasing 3.0% in 2013.

Business spending on structures (nonresidential structures) fell at an annual rate of 1.6% in the second quarter of 2015, its fourth decline in the past five quarters. Business spending on equipment declined at a rate of 4.1% in the second quarter, after rising at a rate of 2.1% in the previous quarter. Business spending on intellectual property products rose for the eighth consecutive month, increasing at a rate of 5.5% in the second quarter. Spending on software and research and development accounted for most of the gain.

Residential fixed investment, often considered a proxy for the housing market, grew at an annual rate of 6.6% during the second quarter of 2015. The second-quarter rate was the slowest since the third quarter of 2013. This quarter’s growth in residential fixed investment added 0.21 percentage point to the second-quarter GDP. Residential fixed investment increased 1.8% in 2014 and 9.5% in 2013.

BUSINESS INVENTORIES

Businesses’ inventory investments decelerated in the second quarter of 2015. Private businesses increased inventories $110.0 billion in the second quarter, following increases of $112.8 billion in the first quarter and $78.2 billion in the fourth. The change in real private inventories subtracted 0.08 percentage point from the second-quarter GDP rate after adding 0.87 percentage point to the first-quarter rate.

EXPORTS AND IMPORTS

Exports rose at a rate of 5.3% in the second quarter of 2015, after falling at a rate of 6.0% in the prior quarter. Exported goods fell at a rate of 6.8% in the second quarter, while exported services rose at a rate of 2.5%. Exports increased 3.4% in 2014 and 2.8% in 2013.

Imports, which are a subtraction in the calculation of GDP, rose at a 3.5% rate in the second quarter after growing at a rate of 7.1% in the previous quarter. Imported goods moved up at a rate of 3.7% in the second quarter, while imported services increased at a rate of 2.5%. Imports increased 3.8% in 2014 and 1.1% in 2013.

Net exports (the value of exports minus the value of imports) added 0.13 percentage point to the second-quarter GDP, after subtracting 1.92 points in the prior quarter.

CONSUMER PRICES AND INFLATION RATES

According to the Bureau of Economic Analysis, the price index for gross domestic purchases rose 1.4% in the second quarter of 2015, compared with a decrease of 1.6% in the previous quarter. The price index for gross domestic purchases measures prices paid by U.S. residents. Excluding food and energy prices, the price index for gross domestic purchases rose 1.1% in the second quarter, compared with an increase of 0.2% in the previous quarter.

Consumer prices rose in June, driven by increasing energy costs, though higher prices for food and shelter also contributed to the rise. The U.S. Department of Labor reported that the Consumer Price Index (CPI) rose 0.3% in June, on a seasonally adjusted basis, its second largest increase in 13 months. Over the last 12 months, CPI has risen 0.1%. CPI is a measure of a basket of products and services—including housing, electricity, food, and transportation—and is used as a measure of inflation. CPI is comprised of three main indexes: the food index, the energy index, and the all items less food and energy index (also known as “Core CPI”).

The energy index rose in June (+1.7%) for the second straight month as the indexes for gasoline, electricity, and natural gas all increased. The gas index, which rose 10.4% in May, climbed 3.4% in June. In June, the food index posted its largest increase since September 2014, increasing 0.3%, partly due to a sharp increase in the eggs index.

Core CPI rose 0.2% in June. The shelter index rose, as did the indexes for recreation, airline fares, personal care, tobacco, and new vehicles. These increases more than offset declines in the indexes for medical care, household furnishings and operations, used cars and trucks, and apparel. Core CPI has risen 1.8% over the past 12 months.

The U.S. Department of Labor reported that the Producer Price Index (PPI) advanced 0.4% in June, on a seasonally adjusted basis, its third increase in the last four months. PPI is down 0.7% over the past 12 months. PPI is a gauge of inflation in the manufacturing process that can be a precursor to inflation in consumer prices. PPI for final demand is comprised of two main indexes: final demand services and final demand goods.

The index for final demand goods increased 0.7% in June, its third increase in 12 months. Approximately 60% of the increase was attributed to prices for energy, which rose 2.4%. The majority of the increase in the energy index came from the gas index, which advanced 4.3%.

Prices for chicken eggs, pharmaceutical preparations, residential electric power, residential natural gas, and cigarettes also rose higher.

The index for final demand services edged up 0.3% in June, its first increase in three months. About 30% of the increase in final demand services prices was the result of prices for loan services, which rose 2.4%. The indexes for machinery and equipment wholesaling, fuels and lubricants retailing, truck transportation of freight, deposit services, and portfolio management also climbed higher.

The index for final demand goods less volatile food and energy prices moved up 0.4% in June, on a seasonally adjusted basis. The index for final demand goods less food and energy remained up 0.6% from one year ago.

ENERGY PRICES

The Energy Information Administration (EIA) reported that the spot price for a barrel of West Texas Intermediate (WTI) crude oil was $59.48 at the end of the second quarter of 2015. This was up from $48.66 per barrel at the end of the first quarter and much lower from one year ago, when the price was $106.07 per barrel.

The regular retail gas price (conventional areas) was $2.64 per gallon at the end of the second quarter, up from the price of $2.35 per gallon at the end of the previous quarter but down significantly from one year ago, when the price was $3.64 per gallon.

The Henry Hub natural gas spot price was $2.80 per million Btu (MMBtu) at the end of the second quarter, up from $2.64 per MMBtu at the end of the previous quarter but well below the price of $4.39 per MMBtu from one year ago.

INTEREST RATES

The Federal Open Market Committee (FOMC) met twice during the second quarter of 2015, issuing a statement from each meeting. At both meetings, the FOMC reaffirmed its desire to keep its target for the federal funds rate near zero. The FOMC’s goal with these decisions is to support its continued progress toward maximum employment and price stability. The federal funds rate is the interest rate at which a commercial bank lends immediately available funds in balances at the Federal Reserve to another commercial bank. The FOMC establishes a target rate and expands or contracts the money supply with the aim that the federal funds rate, a market rate, will approximate the target rate.

The FOMC stated that it would continue to assess a wide range of information in maintaining its current target for the federal funds rate, including measures of labor market conditions, indicators of inflation pressures and inflation expectations, and readings on financial and international developments. The FOMC said it would be appropriate to raise the rate when the labor market improves further and it appears evident that inflation will move closer to 2.0% over the medium term.

The statements read that, while economic activity was little changed in the first quarter, the economy expanded moderately since. It noted that job gains picked up steadily, household spending has been moderate, and the housing sector has shown some improvement. It did note that business spending and net exports have remained soft. Inflation also continued to run below

the FOMC's object, partly reflecting earlier declines in energy prices and decreasing prices of import.

To maintain accommodative financial conditions, the FOMC maintained its existing policy of reinvesting principal payments from its holdings of agency debt and agency mortgage-backed securities.

During the second quarter of 2015, the Board of Governors of the Federal Reserve left the discount rate unchanged, at 0.75%. The discount rate is the interest rate a commercial bank is charged to borrow funds, typically for a short period, directly from a Federal Reserve Bank. The board of directors of each Reserve Bank establishes the discount rate every 14 days, subject to the approval of the Board of Governors.

UNEMPLOYMENT AND PERSONAL INCOME

Job creation continued to improve in June, though the figures for May and April were revised downward. The U.S. economy added 223,000 jobs in June, slightly below the 233,000 forecasted in a Bloomberg survey of economists. There have been 5.6 million jobs created over the past two years, which is the best two-year job growth since 2000. Further, the private sector has added 12.8 million jobs over 64 straight months of job growth, extending the longest streak on record.

Employment increased in professional and business services (+64,000 jobs), healthcare (+40,000), retail trade (+23,000), financial activities (+20,000), and transportation and warehousing (+17,000). Mining employment declined, while employment in other major industries, including construction, manufacturing, wholesale trade, information, and government, showed little or no change in June.

The unemployment rate (also known as the U3 unemployment rate) declined 0.2 point in June to 5.3%, its lowest level since April 2008. The total number of unemployed persons fell by 375,000 in June to 8.3 million. The U3 unemployment rate is the official unemployment rate per the International Labour Organization definition and occurs when people who have actively looked for work within the past four weeks are still without jobs.

The civilian labor force shrunk by 432,000 in June, and the labor-force participation rate moved down by 0.3 percentage point to 62.6%. The employment-population ratio—the share of the working-age population with a job—was essentially unchanged in June at 59.3%. The employment-population ratio has shown little movement so far in 2015.

The number of long-term unemployed (those jobless for 27 weeks or more) dropped by 381,000 in June to 25.8% of the total unemployed. Over the past 12 months, the number of long-term unemployed has declined by 955,000. The average unemployment duration also decreased from one year ago. On average, the unemployed were out of work in June 2015 for 28.1 weeks, compared with 30.7 weeks in June 2014.

If the economy added 191,000 jobs a month, which is the average monthly rate of growth since the jobs recovery began in March 2010, then the Hamilton Project calculates that it will take until August 2017 to close the "jobs gap" left by the recession. As of June 2015, the U.S. had a jobs gap of 3.5 million jobs. The jobs gap is the number of jobs that the U.S. economy needs to create to return to prerecession employment levels while also absorbing the people who enter the labor force each month. At a pace of 245,000 jobs per month, which is the average growth rate

over the last 12 months, the Hamilton Project calculates that it would take until January 2017 to fill the U.S. jobs gap. The Hamilton Project was launched in 2006 as an economic policy initiative at the Brookings Institution. The Hamilton Project is guided by an advisory council of academics, business leaders, and former public policymakers.

The rate of another category of unemployment, U6, dropped 0.3 percentage point in June to 10.5% and is down from the 12.0% rate from one year ago. U6 unemployment is broader than U3 and includes "marginally attached workers" and people who are looking for and want full-time work but have settled for part-time employment. Marginally attached workers are people who are not actively looking for work but who have indicated that they want a job and have looked for work (without success) sometime in the past 12 months. This class also includes "discouraged workers," those who have completely given up on finding a job because they feel that they would be unable to find one.

Both wages and the workweek for private employees were unchanged in June. Average hourly earnings for all private-sector employees were unchanged in June at $24.95. Over the last year, average hourly earnings for all private-sector employees have increased 49 cents, or 2.0%. Average hourly earnings for private-sector production and nonsupervisory employees rose two cents in June to $20.99. Over the last 12 months, average hourly earnings for private-sector production and nonsupervisory employees have increased 40 cents, or 1.9%.

The average workweek for all private workers in June remained at 34.5 hours for the fourth month in a row. The average workweek for production and nonsupervisory employees on private payrolls was unchanged at 33.6 hours. The manufacturing workweek edged down 0.1 hour in June to 40.7 hours, while factory overtime moved up 0.1 hour to 3.4 hours.

The Bureau of Economic Analysis reported that current-dollar personal income increased $145.0 billion in the second quarter of 2015, after increasing by $118.9 billion in the first. The BEA found that the acceleration in personal income primarily reflected upturns in personal interest income and in farm proprietors' income, which was partly offset by decelerations in government social benefits and in personal dividend income.

Personal current taxes increased $26.3 billion in the second quarter, compared with an increase of $60.2 billion in the first.

Disposable personal income increased $118.6 billion (+3.7%) in the second quarter, compared with an increase of $58.7 billion (+1.8%) in the first. Real disposable personal income increased 1.5% in the second quarter, compared with an increase of 3.8% in the first.

Personal outlays increased $161.9 billion in the second quarter, in contrast to a decrease of $10.3 billion in the first. Personal saving—disposable personal income less personal outlays—was $640.1 billion in the second quarter, down from $683.3 billion in the first.

The personal saving rate—saving as a percentage of disposable personal income—was 4.8% in the second quarter, down from 5.2% in the previous quarter.

INDEX OF LEADING INDICATORS

The Conference Board's Leading Economic Index (LEI) advanced 0.6 point in June, following a 0.8-point increase in May. LEI increased at a 4.3% annual rate in the six-month period ending

June 2015, slower than the 6.6% annual rate during the previous six months. Despite the slower rate of growth, the report noted that the strengths among the leading indicators remain more widespread than the weaknesses. The Conference Board found that the recent LEI increases point to a continued strength in the economic outlook for the remainder of the year.

In June, six of the 10 components that comprise LEI increased, while one declined, and three remained unchanged. The positive contributors, beginning with the largest contributor, were the interest rate spread, building permits, average consumer expectations for business conditions, the Leading Credit Index, manufacturers' new orders for nondefense capital goods excluding aircraft, and the ISM new orders index. The stock prices component declined, while average weekly manufacturing hours, average weekly initial claims for unemployment insurance, and manufacturers' new orders for consumer goods and materials were unchanged.

The LEI is a leading American economic indicator intended to forecast future activity. The index is calculated by The Conference Board, a nongovernmental organization, which determines the value of the index from the values of 10 key variables. The 10 components of the LEI include:

- Average weekly hours, manufacturing;
- Average weekly initial claims for unemployment insurance;
- Manufacturers' new orders, consumer goods and materials;
- Institute for Supply Management's Index of New Orders;
- Manufacturers' new orders, nondefense capital goods excluding aircraft orders;
- Building permits, new private housing units;
- Stock prices, 500 common stocks;
- Leading Credit Index;
- Interest rate spread, 10-year Treasury bonds less federal funds; and
- Average consumer expectations for business conditions.

CONSUMER CONFIDENCE

Consumer confidence continued to improve in June. After a moderate rise in May, the Conference Board's Consumer Confidence Index rose 6.8 points in June to a reading of 101.4. The report found that consumers became more confident about the current business and employment conditions over the past two months. Consumers' optimism toward future conditions also improved in June, though their perceptions of their future income prospects were little changed.

Consumers' assessment of current conditions improved in June, as the Present Situation Index rose to 111.6 from 107.1 in May. The percentage of respondents claiming jobs were "hard to get" declined to 25.7% from 27.2% in the prior month, while those claiming that jobs were "plentiful" rose to 21.4% from 20.6%. Those who believed business conditions were "good" improved to 26.4% from 24.7%, while those saying business conditions were "bad" were unchanged at 17.8%.

Consumers' optimism regarding their short-term outlook also increased in June. The Expectations Index advanced to 94.6 from its previous reading of 86.2. The percentage of respondents who expected business conditions to improve over the next six months edged up to 18.5% from 16.0% in the month before, while the percentage of those expecting business conditions to worsen fell to 9.8% from 11.3%.

Consumers' outlook for the labor market was also more positive in June. The percentage of respondents who anticipated more jobs in the months ahead increased to 17.8% from 14.7%, while those anticipating fewer jobs dropped to 15.1% from 16.6%. The share of respondents expecting their incomes to grow was unchanged at 17.5% for the second consecutive month, while the percentage expecting their incomes to decrease moved down slightly to 10.2% from 10.7%.

The Consumer Confidence Index is an indicator designed to measure the degree of optimism about the state of the economy that consumers are expressing through their savings and spending. A month-on-month decreasing trend in the Consumer Confidence Index suggests consumers have a negative outlook on their ability to secure and retain good jobs, whereas a rising trend in consumer confidence indicates improvements in consumer buying patterns. Opinions on current conditions make up 40% of the index (the Present Situation Index), while expectations of future conditions comprise the remaining 60% (the Expectations Index).

Consumer sentiment rose in June and more than erased its decline in May. The Thomson Reuters/University of Michigan's Consumer Sentiment Index rose 5.4 points in June to a reading of 96.1. The survey found that the first half of 2015 has been the largest and most sustained increase in economic optimism since 2004. Importantly, the record was true for households in the top third, middle, and bottom third of the income distribution.

The Expectations Index rose 3.6 points in June to 87.8, while the Current Conditions Index climbed 8.1 points to 108.9. The data continued to indicate that consumer spending is expected to grow 3.0% in 2015.

In June, the fewest percentage of consumers since August 2000 believed the economy had worsened. Consumers reported hearing fewer recent job losses, and most anticipated the economy would improve over the year ahead. When consumers' expectations for the economy were averaged over the first half of 2015, they were more favorable than in the first half of any other year since 2000.

In the first six months of 2015, consumers assessed their current finances and future financial prospects more favorably than in the first half of any other year since 2007. However, the favorable expectations were driven by low income expectations, as households expected a 1.5% income increase, down from 2.5% in the first half of 2007. It was a lower prevailing inflation rate that made real income gains higher in the first half of 2015 than at any time since the first half of 2007.

The Thomson Reuters/University of Michigan's Survey of Consumers is a rotating panel survey based on a nationally representative sample that gives each household in the contiguous U.S. an equal probability of being selected. Interviews are conducted by telephone throughout the month. The Index of Consumer Sentiment is composed of the Expectations Index and the Current Conditions Index and is intended to gauge how consumers feel the economic environment will change. The survey's Index of Consumer Expectations is an official component of the U.S. Leading Economic Index.

BUSINESS OPTIMISM

Business owners were more pessimistic in June, ending a five-month streak of increasing optimism. The National Federation of Independent Business (NFIB) reported that the Small Business Optimism Index fell by 4.2 points in June to 94.1. The decline was widespread among the index's components, as nine of the 10 components fell, and one remained unchanged.

A decline in the component that measures business owners' spending plans accounted for 30% of the index's decline, and a deterioration in the component for earnings trends accounted for 25%. A decline in the components that measure owners' expectations for real sales and business conditions, together, accounted for another 20% of the decline. Owners' plans to raise pay were also bleak. A seasonally adjusted net 11.0% of small business owners planned to raise compensation in the coming months, the lowest reading since October 2013.

The Small Business Optimism Index is compiled from a survey of the NFIB's 350,000 members that it conducts each month. NFIB, founded in 1943, began conducting its survey quarterly in 1974, transitioning to a monthly survey in 1986. The index is a composite of 10 seasonally adjusted components based on questions about the following: plans to increase employment, plans to make capital outlays, plans to increase inventories, whether members expect the economy to improve, whether they expect real sales will be higher, current inventory, current job opening, expected credit conditions, whether now is a good time to expand, and earnings trend. Analysts watch the index because small businesses are responsible for the majority of new job creation and the NFIB focuses on this sector of the economy.

The 2Q 2015 Wells Fargo/Gallup Small Business Index dipped 7.0 points to a reading of 64.0, representing the first significant decrease since November 2012. Small declines in how business owners regard their business's financial situation, most notably current revenues, lead the downturn. The second-quarter Small Business Index score is still considerably higher than it was in the second quarter of 2014, when the score was 47.0, and in 2013, when the reading was 16.0. The Present Situation Index—how business owners rate current conditions for their businesses—declined 4.0 points to 24.0. The Expectations Index—how business owners expect conditions to be over the next 12 months—dropped 3.0 points to 40.0.

The report found that 42.0% of small-business owners reported that their revenues increased over the past 12 months, down from 49.0% in the prior survey. However, this was up from 36.0% one year ago.

Owners reported increased cash flow, with 58.0% of owners rating their company's cash flow as somewhat good or very good over the past 12 months, up from 54.0% in the previous survey and 50.0% one year ago. The percentage of business owners reporting good current cash flow is the highest since the first quarter of 2008.

The survey found that 65.0% of owners rated their company's financial situation as very or somewhat good. While this was unchanged from the prior survey, it was up from 57.0% one year ago.

Since August 2003, the Wells Fargo/Gallup Small Business Index has surveyed small-business owners on current and future perceptions of their business's financial situation. The Small Business Index is published once a quarter. The Small Business Index consists of owners' ratings of their business's current situation and their expectations for the next 12 months, measured in

terms of their overall financial situation, revenue, cash flow, capital spending, number of jobs, and ease of obtaining credit. Prior to the recession and financial crisis of 2008-2009, Small Business Index scores were generally in triple digits. The Small Business Index reached its peak of 114.0 in December 2006 and hit its low point of -28.0 in July 2010.

STOCK MARKETS AND VOLATILITY

The blue chip stocks comprising the Dow Jones Industrial Average gave up some ground in the second quarter. T. Rowe Price found that relief over corporate earnings growth and enthusiasm about a reaccelerating U.S. economy were dragged down by worries over the ongoing Greek debt crisis. The S&P 500 saw a negative price return for the quarter but was boosted by dividends to a positive total return. The Nasdaq, boosted by merger and acquisition activity, managed to break the record high it established in 2000, before pulling back a bit at the end of the quarter. The smaller-cap indexes experienced mixed performance in the second quarter, with small-cap stocks outperforming the large-cap stocks, while midcaps performed the worst among the major benchmarks. Utilities and industrials shares were the poorest performing sectors within the S&P 500 Index, while healthcare and consumer discretionary shares were the best performing.

The Dow Jones Industrial Average (Dow) fell 0.9% in the second quarter. Including dividends, the Dow's total return was -0.3% in the second quarter, according to T. Rowe Price. The Dow is an index of 30 of the largest and most widely held public companies in the U.S. and is considered the most-watched index in the world.

The Nasdaq Composite index (Nasdaq), consisting mainly of high-tech stocks, rose 1.8% in the second quarter, on both a price and total return basis, and is up 5.3% so far this year.

The S&P 500 dropped 0.2% in the second quarter. Including dividends, the S&P 500's total return was 0.3% in the second quarter and 1.2% year-to-date. The S&P 500 consists of a representative sample of 500 leading companies of the U.S. economy and is one of the most commonly used benchmarks for the overall U.S. stock market.

The S&P MidCap 400 index slipped 1.4% in the second quarter. The total return for the S&P MidCap 400 was -1.1% in the second quarter but a positive 4.2% year-to-date. The S&P MidCap 400, which is distinct from the large-cap S&P 500, measures the performance of midsized companies and is the most widely followed midcap index.

The Russell 2000 Index grew 0.1% this quarter. The total return for the Russell 2000 was 0.4% in the second quarter and 4.8% thus far in 2015. The Russell 2000 Index serves as a benchmark for small-cap stocks in the U.S. stock market.

Market volatility remained fairly mild in the second quarter. The Chicago Board Options Exchange Volatility Index (VIX)—a popular volatility measure—reached a high of 18.9 in the second quarter but averaged 13.7. This was comparable to the high of 22.4 and average of 16.6 in the previous quarter.

The VIX represents the implied volatility of 30-day options on the Standard & Poor's 500 stocks and has been termed by analysts and investors as the "fear gauge." Accordingly, the VIX represents the expected volatility of the market, as represented by the S&P 500. Stock market professionals use the VIX to gauge investor sentiment. Values greater than 30 are generally

associated with a large amount of volatility as a result of investor fear or uncertainty, while values below 20 generally correspond to less stressful, even complacent, times in the markets.

BOND MARKETS

T. Rowe Price reported that U.S. Treasuries posted their first quarterly loss since 2013, as fears of an imminent Federal Reserve rate increase outweighed demand for safe-haven assets as Greece moved toward default. The yield on the 10-year Treasury rose from 1.87% at the start of April to almost 2.50% in June, its highest level in 2015, before declining slightly by the end of the quarter. (Bond prices and yields move in opposite directions.) T. Rowe Price also noted that the Treasury yield curve steepened as longer-term yields rose more than shorter-term rates, with the 30-year Treasury's yield increasing more than 50 basis points.

The 30-day T-bill rate was 0.02% at the end of the second quarter of 2015, little changed from 0.05% at the end of the first quarter. The five-year Treasury ended the second quarter with a yield of 1.63%, up from 1.37% at the end of the previous quarter.

The 10-year Treasury bond yield increased to 2.35% at the end of the second quarter from a yield of 1.94% at the end of the first. The 20-year Treasury bond yield rose to 2.83% at the end of the second quarter from 2.31% at the end of the first.

Moody's seasoned Aaa and Baa corporate bonds ended the second quarter with a yield of 4.19% and 5.18%, respectively, up from yields of 3.52% and 4.49% at the end of the previous quarter.

The prime lending rate was 3.25% at the beginning of the second quarter and remained there through the end of June. The discount window (primary credit) remained at 0.75% during the second quarter.

CONSTRUCTION

Housing starts and building permits rose in June and well exceeded their levels from a year ago, driven by a surge in multifamily housing. According to the U.S. Census Bureau, privately owned housing starts in June were at a seasonally adjusted annual rate of 1,174,000, up 9.8% from the previous month, 26.6% above their level from one year ago. The construction of single-family homes retreated 0.9% in June but was up 14.7% from one year ago. The construction of multifamily homes soared 28.6% in June and was up 55.0% above its levels from one year ago. The multifamily home sector, which consists of buildings with five units or more, tends to be more volatile than the single-family home sector.

Building permit authorizations for privately owned housing units, considered a good leading indicator of demand for new homes, were at a seasonally adjusted rate of 1,343,000 in June. This was 7.4% above the rate in the prior month and 30.0% from the rate from one year ago. Building permits for single-family housing units rose 7.4% in June and were up 30.0% from one year ago. Building permits for multifamily housing units increased 16.1% in June and were up a sizable 79.0% from one year ago.

The U.S. Census Bureau reported that overall spending on construction was at a seasonally adjusted annual rate of $1,064.6 billion in June. This figure was 0.1% above the May rate of $1,063.5 billion and 12.0% above the $950.3 billion rate from one year ago. Overall construction

spending amounted to $482.7 billion in the first six months of 2015, 8.0% above the $446.8 billion spent during the same period in 2014.

Spending on all private construction was at a seasonally adjusted annual rate of $766.4 billion in June, 0.5% below the May rate of $770.0 billion but 13.7% above the rate from one year ago. Private residential construction spending was at a seasonally adjusted annual rate of $371.6 billion in June, 0.4% above the rate of $370.0 billion in May and 12.8% above the rate from one year ago. Private nonresidential construction was at a seasonally adjusted annual rate of $394.8 billion in June, down 1.3% from the May rate of $400.0 billion but 14.6% above the rate from a year ago.

The total amount spent on private construction was $354.5 billion during the first six months of 2015, up 9.1% from the same period in 2014. Spending on residential construction was $173.0 billion during the first six months of 2015, up 8.5% from the amount spent during that same period in 2014. Spending on nonresidential private construction was $181.4 billion in the first six months of 2015, up 9.7% from the amount spent during the period in 2014.

The seasonally adjusted annual rate of total public construction spending was $298.2 billion in June, up 1.6% from the May rate of $293.5 billion and 8.0% above the rate from a year ago. Educational construction was at a seasonally adjusted annual rate of $67.2 billion in June, 0.2% above the May rate of $67.1 billion and 3.6% above the rate from a year ago. Highway and street construction was at a seasonally adjusted annual rate of $90.9 billion in June, 1.2% above the May rate of $89.8 billion, and 14.2% above the rate from one year ago.

The total amount spent on public construction was $128.2 billion in the first six months of 2015, up 5.3% from the same period in 2014. Spending on educational construction was $30.2 billion during the first six months of 2015, 4.4% above the amount spent during that period in the previous year. Spending on highway and street construction was $34.8 billion during the first six months of 2015, up 4.6% from the amount spent during that same period in 2014.

MANUFACTURING

The Federal Reserve reported that total industrial production increased 0.3% in June, after falling 0.2% in May and declining 0.5% in April. Industrial production fell at a rate of 1.4% in the second quarter but remained up 1.5% from a year ago. Industrial production is an output measure of the industrial sector of the economy. The industrial sector includes manufacturing, mining, and utilities, with manufacturing accounting for approximately 75% of total industrial production.

Manufacturing output was unchanged in June, as a downturn in durable goods manufacturing offset a slight increase in nondurable goods manufacturing. Within nondurables manufacturing, chemicals and products posted the largest rise at 0.7%, while all of the other major industries saw gains or losses of less than 0.5%. Among the durable goods industries, the indexes for motor vehicles and parts and for wood products dropped notably, while the indexes for computer and electronic products, for furniture and related products, and for miscellaneous manufacturing each rose substantially. Manufacturing increased at an annual rate of 1.4% in the second quarter of 2015.

The output of utilities rose 1.5% in June but fell at an annual rate of 13.5% in the second quarter of 2015. The mining index rose 1.0% in June, as an increase in crude oil extraction offset a drop

in the index for oil and gas well drilling. The index for oil and gas well drilling has fallen for seven consecutive months, though the June decrease of approximately 3.0% was the smallest since December. For the second quarter of 2015, mining output retreated at an annual rate of 5.7%.

Industrial capacity utilization advanced 0.2 percentage point in June to 78.4%. Capacity utilization is the percentage of production capacity manufacturers actually use. The June capacity utilization rate is 2.6 percentage points above its level from a year ago but 1.7 percentage points below its long-run average between 1972 and 2014.

The U.S. Census Bureau announced that new orders for manufactured durable goods rose $7.7 billion (3.4%) in June to $235.3 billion. June's increase in new orders followed a 2.1% decline in May and a 1.7% decrease in April. Excluding defense, new orders increased 3.8% in June after falling 2.4% in May. Excluding the volatile transportation orders, new orders rose 0.8% in June after edging down 0.1% in May. Orders for transportation equipment increased 8.9% in June after falling 6.1% in May and declining 4.0% in April. New orders for nondefense capital goods excluding volatile aircraft orders—an indicator of business spending strength—rose 0.9% in June after dropping 0.4% in May and falling 0.7% in April.

The manufacturing sector grew in June at its fastest pace in five months. The Institute for Supply Management (ISM) reported that its Manufacturing Index (PMI) rose 0.7 percentage point in June to a reading of 53.5%. PMI is an indicator of the economic health of the manufacturing sector and is based on data compiled from purchasing and supply executives nationwide.

A reading above 50% indicates that the manufacturing economy is generally expanding; a reading below 50% indicates that it is generally contracting. A PMI in excess of 43.1%, over a period of time, generally indicates an expansion of the overall economy. Therefore, the June PMI indicates an expansion in the manufacturing sector for the 30th consecutive month and growth in the overall economy for the 73rd consecutive month.

The panels' comments indicated that business conditions were mostly stable or improving, with the notable exception of the oil and gas markets. Also noted was the negative effect on egg prices and availability due to the avian flu outbreak.

Of the 18 manufacturing sectors surveyed in June, 11 reported growth. The report stated that, based on the past relationship between PMI and the overall economy, the average PMI for January through June (52.6%) corresponds to a 3.0% increase in GDP on an annualized basis. In addition, if PMI for June (53.5%) were annualized, it would correspond to a 3.3% increase in real GDP annually.

The component for new orders improved 0.2 percentage point in June to 56.0% and indicated that new orders grew for the 31st consecutive month. A New Orders Index above 52.1%, over time, is generally consistent with an increase in the Census Bureau's series on manufacturing orders.

The component for production slipped 0.5 percentage point in June to 54.0% but remained at a level that indicated production grew for the 34th consecutive month. An index above 51.1%, over time, is generally consistent with an increase in the Federal Reserve Board's industrial production figures.

Manufacturing employment increased 3.8 percentage points in June to a reading of 55.5%, indicating growth in employment for the second consecutive month. An Employment Index above 50.6%, over time, is generally consistent with an increase in the Bureau of Labor Statistics' data on manufacturing employment.

The index that tracks inventory moved up 1.5 percentage points in June to 53.5%, indicating raw materials inventories grew for the second month in a row. An Inventories Index greater than 42.9%, over time, is generally consistent with expansion in the Bureau of Economic Analysis's figures on overall manufacturing inventories.

The component that measures prices was unchanged in June at 49.5%, remaining at a level indicating a decrease in raw materials prices for the eighth straight month. In June, 14.0% of respondents reported paying higher prices, 15.0% reported paying lower prices, and 71.0% reported paying the same prices. A Prices Index above 49.7%, over time, is generally consistent with an increase in the Bureau of Labor Statistics' Index of Manufacturers Prices.

SERVICES

The services sector expanded in June at a slightly faster rate than in the previous month. The ISM reported that its Non-Manufacturing Index (NMI) rose 0.3 percentage point in June to 56.0%. NMI measures the strength of the services sector and is based on data compiled from purchasing and supply executives nationwide.

A reading above 50% indicates that the services sector of the economy is generally expanding, whereas a reading below 50% indicates that the services sector is generally contracting. An NMI in excess of 48.7%, over a period of time, generally indicates an expansion in the overall economy. Therefore, the June NMI indicates an expansion in the services sector for the 65th consecutive month and growth in the overall economy for the 71st consecutive month.

Of the 18 nonmanufacturing sectors surveyed in June, 15 reported growth. The majority of the respondents' comments were positive about the economy and business conditions.

The component that measures business activity rose 2.0 percentage points in June to 61.5% and indicated that business activity grew for the 71st consecutive month. The new orders component of the index edged up 0.4 percentage point to 58.3%, signaling growth in new orders for the 71st straight month. The employment component fell 2.6 percentage points in June to 52.7% but remained at a reading signifying employment in the services sector grew for the 16th consecutive month.

REAL ESTATE

National Association of Home Builders

Builder confidence rose significantly in June as builders reported more serious and committed buyers. The National Association of Home Builders (NAHB)/Wells Fargo Housing Market Index (HMI) improved 5.0 points in June to 59.0, its highest reading since September 2014. An HMI reading above 50.0 indicates that more builders view sales conditions as good, rather than poor. The HMI components that measure current and future sales expectations hit their highest levels since the fourth quarter of 2005, as optimism among builders grew that the housing market

would continue to strengthen. HMI has now been above the 50-point benchmark for 12 consecutive months.

All three HMI components improved notably in June. The component that measures future sales expectations rose 6.0 points to 69.0. The index that measures buyer traffic advanced 5.0 points to 44.0, and the component that gauges current sales conditions jumped 7.0 points to 65.0.

The HMI three-month moving average in the South and Northeast each rose 3.0 points to 60.0 and 44.0, respectively. The West advanced 2.0 points to 57.0, while the Midwest slipped 1.0 point to 54.0.

National Association of Realtors

The National Association of Realtors (NAR) reported that existing-home sales rose in June to their highest level in over eight years. All of the regions saw sales increases in June and have now been above year-over-year levels for six consecutive months. Rising demand and a limited housing supply helped push the national median sales price to an all-time high.

Existing-home sales rose 3.2% in June to an annual pace of 5.49 million sales from 5.32 million in May, its fastest pace since February 2007. Sales have now increased year-over-year for nine consecutive months and are 9.6% above a year ago. Existing-home sales are completed transactions that include single-family houses, townhomes, condominiums, and co-ops.

Home sales in the Northeast jumped 4.3% in June and were up 12.5% from one year ago. Sales in the Midwest climbed 4.7% in June and were 12.7% above their levels from a year ago. Sales in the South increased 2.3% and are up 7.3% from one year ago. Sales in the West rose 2.5% and are up 8.8% from one year ago.

The national median existing-home price for all housing types was $236,400 in June, up 6.5% from a year ago and higher than the peak median sales price set in July 2006 ($230,400). This marked the 40th consecutive month of year-over-year price gains. In June, home prices in the Northeast improved 3.9% from one year ago, while prices in the Midwest jumped 7.2%. Home prices in the South and West rose 7.2% and 9.9%, respectively, over the last 12 months.

Distressed homes dipped to 8% in June (matching an August 2014 low) from 10% in May and are below 11% from one year ago. Distressed homes include foreclosures and short sales, which are generally sold at deep discounts. In June, 6% of home sales were foreclosures and 2% were short sales. June foreclosures sold for an average discount of 15% below market value, and short sales sold at an average discount of 18%.

With demand continuing to exceed supply, properties continued to sell quickly in June. The median time on the market for all homes sold in June was 34 days, the shortest time since NAR began tracking in 2011. The median time on the market for short sales in June was 129 days, while foreclosures typically sold in 39 days and nondistressed homes took 33 days. In June, 47% of all homes on the market sold in less than a month.

Total housing inventory edged up 0.9% in June to 2.30 million existing homes available for sale and was 0.4% higher than one year ago. Unsold inventory was at a 5.0-month supply at the current sales pace in June, down from 5.1 months in May.

NAR reported that, according to Freddie Mac, the national average commitment rate for a 30-year, conventional, fixed-rate mortgage moved up to 3.98% in June from 3.84% in May. This was the seventh straight month that the rate was below 4.00%.

NAR's Realtors Confidence Index (RCI) report for current conditions showed little change for the various property types. The RCI for single-family homes was unchanged in June, remaining at a reading of 73.0. The RCI for townhouses and condos each rose 1.0 point to 53.0 and 48.0, respectively (strong = 100; moderate = 50; weak = 0). Regardless, the indexes for the three housing types remain well above their levels from one year ago. The RCI is a key indicator of housing market strength based on a monthly survey of over 50,000 real estate practitioners.

Pending home sales dropped slightly in June, ending a string of five monthly increases. Despite the drop, pending home sales in June remain close to that of May, which was the highest level in over nine years. NAR's Pending Home Sales Index (PHSI), a forward-looking indicator based on contract signings, edged down 1.8 points in June to a reading of 110.3. Despite the decline, the index has now increased year-over-year for 10 consecutive months.

The PHSI in the Northeast inched up 0.4 point in June to 94.3 and remained 12.0 points above its level from one year ago. The Midwest index slipped 3.0 points in June to 108.1 but was 5.0 points above its level from a year ago. The South index fell 3.0 points in June to a reading of 123.5 but remained 7.8 points higher than its level from a year ago. The West index moved up 0.5 points in June to 104.4 and was 10.4 points above its reading from one year ago.

The PHSI is an indicator for the housing sector, based on pending sales of existing homes. A sale is listed as pending when the contract has been signed but the transaction has not closed, though the sale usually is finalized within one or two months of signing. There is a closer relationship between annual index changes (from the same month a year earlier) and year-ago changes in sales performance than with month-to-month comparisons. An index of 100 is equal to the average level of contract activity during 2001, which was the first year to be examined, as well as the first of five consecutive record years for existing-home sales.

NAR released its most recent Commercial Real Estate Market Survey, analyzing the second quarter of 2015. The report found that the market maintained an upbeat pace of sales, and respondents reported that fundamentals and investment sales improved. Commercial sales volumes rose 9.1% from a year ago, and 60.0% of NAR members closed a sale.

Commercial inventory remained short and was the No. 1 concern among NAR members. The shortage of inventory caused price growth to accelerate in the second quarter, averaging 6.6% higher than the same period in 2014. The average transaction price rose from $1.7 million in the first quarter of 2015 to $2.0 million in the second. The second highest concern among NAR members was the perceived pricing gap between sellers and buyers.

Average capitalization rates declined to 7.5%, with apartments posting the lowest capitalization rate at 6.8%, followed by hotels at 7.4%. Office and industrial spaces posted average cap rates of 7.7% and 7.5%, respectively. Retail had the highest cap rate at 8.0%.

NAR members were positive about the general direction of business opportunities, which is a broad market indicator tracked by NAR. Business opportunities accelerated in the second quarter, increasing 6.4%, following a 3.8% improvement in the first quarter.

Leasing volume rose 4.7% in the second quarter, and leasing rates advanced 2.7%. The report noted that 54% of NAR members completed a lease transaction. Tenant demand was the greatest in the 5,000-square-foot-or-less space, accounting for 84.0% of all leased properties. Lease terms remained consistent, with 36-month and 60-month leases accounting for 60.0% of the market.

Vacancy rates declined for most property types in the second quarter. The exception to this was apartments, where added supply pushed the vacancy rate up to 6.6% from 6.0% in the same period in 2014. Office vacancies moved down 65 basis points to 15.9% when compared to the same period a year ago. Industrial availability declined the most from a year ago, with the vacancy rate falling 246 basis points to 10.8%. Retail vacancies fell 137 basis points from a year ago to 13.2%.

Lease concessions declined 8.1% in the second quarter, and tenant improvements averaged $10 per square foot per year nationally. Office properties, with high vacancies, recorded the highest tenant improvements at $17 per square foot. Apartments, with low vacancies, posted the lowest tenant improvements at only $3 per square foot.

Homeownership Rates, Homeowner Vacancy Rates, and Rental Vacancy Rates

The U.S. Census Bureau found that the homeownership rate was 63.4% in the second quarter of 2015, down slightly from a rate of 63.7% in the first quarter and below the 64.7% rate from one year ago. The national vacancy rate for rental housing was 6.8% in the second quarter of 2015, a retreat from 7.1% in the first quarter. Rental vacancy is down from this time one year ago, when the rate was 7.5%. The national vacancy rate for homeowners was 1.8% in the second quarter, down somewhat from 1.9% in the prior quarter and from 1.9% a year ago.

Mortgage Bankers Association

The Mortgage Bankers Association (MBA) found that the housing market recovery shifted into a higher gear. As a result, the MBA revised upward its forecasts for home sales and home prices, while its expectations for cash purchases declined. Because of this, the MBA believes mortgage originations in 2015 and 2016 will be greater than was previously predicted.

The MBA believes purchase originations will rise to $801.0 billion in 2015 from its prior expectation of $730.0 billion. It then believes purchase originations will increase to $885.0 billion in 2016. The MBA believes refinance originations will be $551.0 billion in 2015, up from $484.0 billion in 2014. The MBA believes total originations will be $1.35 trillion in 2015 and $1.26 trillion in 2016, compared with $1.12 trillion in 2014.

National Association of Real Estate Investment Trusts

Investment returns for properties, as measured by the National Association of Real Estate Investment Trusts (NAREIT), were virtually all negative in the second quarter after a significantly better first quarter.

National Council of Real Estate Investment Fiduciaries

Property index returns, as measured by the National Council of Real Estate Investment Fiduciaries (NCREIF), were positive in the second quarter. Of the property-type indexes,

industrial properties had the best second-quarter returns, followed by hotels. Of the regional indexes, the West outperformed the others.

The NCREIF Property Index (NPI) is a quarterly time series composite total rate of return measure of investment performance of a very large pool of individual commercial real estate properties acquired in the private market for investment purposes only. All properties in the NPI have been acquired, at least in part, on behalf of tax-exempt institutional investors—the great majority being pension funds. As such, all properties are held in a fiduciary environment.

ECONOMIC OUTLOOK

Consensus Economics Inc., publisher of *Consensus Forecasts—USA*, reports that the consensus of U.S. forecasters is that real GDP will increase at a seasonally adjusted annual rate of 3.2% in the third quarter of 2015 and 3.0% in the fourth quarter. Every month, Consensus Economics surveys a panel of 30 prominent U.S. economic and financial forecasters for their predictions on a range of variables, including future growth, inflation, current account and budget balances, and interest rates. The forecasters expect GDP to grow 2.2% in 2015, 2.8% in 2016, and 2.8% again in 2017.

They forecast consumer spending will increase at a rate of 3.2% in the third quarter of 2015 and 3.1% in the fourth quarter. They expect consumer spending to increase 2.9% in both 2015 and 2016.

These forecasters believe unemployment will average 5.3% in the third quarter of 2015 before ticking down to 5.2% in the fourth quarter. They believe unemployment will average 5.4% in 2015 before declining to 5.0% in 2016.

The forecasters believe the three-month Treasury bill rate will be 0.2% at the end of the third quarter of 2015 and 0.5% at the end of the fourth quarter. They forecast the three-month Treasury bill rate will rise to 0.7% at the end of the first quarter of 2016 and to 1.7% at the end of 2016. They forecast the 10-year Treasury bond yield will be 2.3% at the end of the third quarter of 2015 and 2.5% at the end of the fourth quarter. They believe the 10-year Treasury bond yield will rise to 2.7% at the end of the first quarter of 2016, then to 3.2% at the end of 2016.

They also believe consumer prices will rise at a rate of 2.0% in both the third and fourth quarters of 2015. They expect consumer prices to increase 0.2% in 2015 before rising to 2.1% in 2016. They expect producer prices to rise at a rate of 1.7% in the third quarter of 2015 before increasing at a rate of 2.1% in the fourth quarter. The forecasters anticipate producer prices will drop 2.5% in 2015 but will increase 2.8% in 2016.

The forecasters in the survey believe real disposable personal income will rise at a rate of 2.3% in the third quarter of 2015 and 2.5% in the fourth. They believe real disposable personal income will increase 3.4% in 2015 and 2.5% in 2016.

The forecasters expect industrial production to increase at a rate of 2.8% in the third quarter of 2015 before picking up to a rate of 3.1% in the fourth quarter. They forecast industrial production will increase 2.3% in 2015 and 3.0% in 2016.

Nominal pretax corporate profits will rise 0.5% in 2015, before increasing 4.4% in 2016, according to the forecasters. The forecasters project housing starts will be 1,090,000 in 2015 and 1,270,000 in 2016.

The most recent release of The Livingston Survey (the Survey) predicts higher output growth and lower unemployment for the second half of 2015 than was expected in the prior survey. The Survey, conducted by the Federal Reserve Bank of Philadelphia, is the oldest continuous survey of economists' expectations. It summarizes the forecasts of economists from industry, government, banking, and academia. The participants project real GDP to grow at an annual rate of 3.1% in the second half of 2015 and 2.9% in the first half of 2016. They believe GDP will grow 2.5% annually over the next 10 years.

The Survey forecasted the unemployment rate to be 5.1% in December 2015, before declining to 5.0% in June 2016.

The forecasters in the Survey expect consumer price inflation (CPI) to be 0.1% in 2015 and 2.1% in 2016. The Survey expects CPI to average 2.2% over the next 10 years. The Survey expects producer price inflation (PPI) to be -3.2% in 2015 and 1.9% in 2016.

The Survey predicts the interest rate on three-month Treasury bills will be 0.59% at the end of December 2015. The forecasters predict that the rate will increase to 1.11% in June 2016 and 1.50% in December 2016. They predict the interest rate on 10-year Treasury bonds will reach 2.50% at the end of December 2015. According to the Survey, the rate will then rise to 2.84% in June 2016 and to 3.00% in December 2016.

The forecasters from the Survey have decreased their previous projections for future S&P 500 values. They expect the S&P 500 will be at 2,158.0 at the end of December 2015, before rising to 2,218.0 by the end of June 2016 and 2,243.0 at the end of December 2016.

The Energy Information Administration predicts that the West Texas Intermediate crude oil spot price will average approximately $49.62 per barrel in 2015 and $54.42 per barrel in 2016, compared with $93.17 per barrel in 2014. The EIA expects retail prices for regular-grade gas to average $2.41 per gallon in 2015 and $2.40 per gallon in 2016, down from $3.36 per gallon in 2014.

The Energy Information Administration believes the Henry Hub natural gas spot price will average $2.89 per million Btu (MMBtu) in 2015 and $3.21 per MMBtu in 2016, down from $4.39 per MMBtu in 2014. The cost of coal delivered to electric generating plants, which averaged $2.36 per MMBtu in 2014, is expected to average $2.28 per MMBtu in both 2015 and 2016. Residential electric prices, which averaged 12.50 cents per kilowatt-hour (kWh) in 2014, are expected to rise to 12.74 cents per kWh in 2015 and 13.03 cents per kWh in 2016. The airline ticket price index, which averaged 307.7 in 2014, is expected to fall to 300.6 in 2015 before climbing to 309.7 in 2016.

The National Association of Realtors' Realtors Confidence Index for future conditions lost ground for all property types in June but remained above levels from one year ago. The RCI for the outlook of single-family homes and townhomes each slipped 2.0 points to 72.0 and 53.0, respectively, while the figure for condos shed 1.0 point to 49.0 (strong = 100; moderate = 50; weak = 0). The RCI is a key indicator of housing market strength based on a monthly survey of

over 50,000 real estate practitioners. Practitioners are asked about their expectations for home sales, prices, and market conditions.

NAR believes existing-home sales will be 5.263 million (+6.5%) in 2015 and 5.500 million (+4.5%) in 2016. It believes new single-family home sales will be 574,000 (+30.8%) in 2015, before increasing to 730,000 (+27.2%) in 2016. NAR believes the median existing-home price will be $222,700 (+6.9%) in 2015, before increasing to $232,000 (+4.2%) in 2016. NAR believes the median new-home price will increase to $293,800 (+3.9%) in 2015, before rising to $305,000 (+3.8%) in 2016. It expects housing starts to increase to 1,127,000 (+12.6%) in 2015, then to 1,380,000 (+22.4%) in 2016. NAR believes the 30-year fixed mortgage rate will average 4.0% in 2015, before rising to 4.8% in 2016, and the one-year adjustable rate will average 2.6% in 2015 and 4.0% in 2016.

The most recent three-year outlook from the Urban Land Institute (ULI) and Ernst & Young (EY) found that real estate economists and analysts believe the real estate industry will remain on a sustainable course of solid growth for 2015 through 2017. The *ULI/EY Real Estate Consensus Forecast,* a semiannual publication, is based on a survey of 46 of the industry's top economists and analysts representing 33 of the country's leading real estate investment, advisory, and research firms and organizations. The forecast for each indicator is the median forecast from the 43 survey respondents. The key findings from the *Real Estate Consensus Forecast* include:

- Net job growth is expected to be 2.9 million per year, and demand for real estate, particularly office and apartments, will remain strong. Low unemployment rates will lead to improved wage growth, but shortages of skilled workers may arise.

- The rate for 10-Year U.S. Treasury notes will average 3.0% between 2015 and 2017, lower than the long-term average of 4.1%, but will rise significantly over the forecast period.

- Issuance of commercial mortgage-backed securities is projected to rise to $150 billion in 2017 (rising from $115 billion in 2015 and $133 billion in 2016). With banks and insurance companies also active, real estate lending will remain competitive and favorable for borrowers.

- Commercial real estate prices, as measured by the Moody's/RCA Index, are expected to rise by an average of 7.6% per year, compared to a long-term average increase of 5.3%, implying three strong years of net appreciation for U.S. real estate.

- Warehouse rents and hotel revenue per available room (RevPAR) are expected to lead the major property types, growing by an average of 3.6% and 5.3%, respectively, between 2015 and 2017. This is significantly greater than their historical growth rates.

- The total return rate for core unleveraged properties, as measured by the National Council of Real Estate Investment Fiduciaries (NCREIF), is expected to average 9.9% between 2015 and 2017, which is significantly higher than the expected average yield for U.S. Treasuries.

The *Real Estate Consensus Forecast* findings for each commercial property type are:

- *Apartments:* Vacancy rates for apartments are forecasted to rise modestly from 4.6% in 2014 to 4.7% in 2015, 5.0% in 2016, and 5.3% in 2017. Survey respondents expect rental rates to rise by 3.5% in 2015, 3.0% in 2016, and 2.7% in 2017. NCREIF total annual returns for the apartment sector are expected to be 9.0% in 2015, 8.3% in 2016, and 8.0% in 2017.

- *Industrial/warehouse:* Availability rates for the industrial/warehouse property type are forecasted to drop from 10.3% in 2014 to 9.8% in 2015 and to 9.6% for both 2016 and 2017. Survey respondents expect rental rates to rise by 4.0% in 2015, 3.8% in 2016, and 3.1% in 2017. NCREIF total annual returns for the industrial sector are projected to be 12.0% in 2015, 10.5% in 2016, and 9.5% in 2017.

- *Office:* The forecast predicts office vacancy rates to continue their decline, dropping from 13.9% in 2014 to 13.0% in 2015, 12.5% in 2016, and 12.0% by the end of 2017. Survey respondents project rental rates to rise by 4.0% in 2015, 4.1% in 2016, and 3.5% in 2017. NCREIF total annual returns for the office sector are forecasted to be 11.8% in 2015, 10.0% in 2016, and 9.0% in 2017.

- *Retail:* The respondents forecast retail availability rates to drop from 11.4% in 2014 to 10.9% in 2015, 10.5% in 2016, and 10.2% in 2017. Rental rates are projected to rise by 2.0% in 2015, 3.0% in 2016, and 2.9% in 2017. NCREIF total annual returns for the retail sector are projected to be 10.9% in 2015, 10.0% in 2016, and 8.4% in 2017.

- *Hotel:* The forecasters expect hotel occupancy rates to rise from 64.4% in 2014 to 65.2% in 2015 and to 65.6% in both 2016 and 2017. RevPAR rates are expected to rise 7.0% in 2015, 5.0% in 2016, and 4.0% in 2017.

The forecasters in the *ULI/EY Real Estate Consensus Forecast* expect housing starts to rise from 647,400 in 2014 to 700,000 in 2015, 815,000 in 2016, and 900,000 by the end of 2017. They forecast that the average price for existing homes in the U.S. will rise by 5.0% in 2015, 4.0% in 2016, and 4.0% in 2017.

Historical Economic Data 2011-2014 and Forecasts 2015-2024

	Historical Data				Consensus Forecasts**					
	2011	**2012**	**2013**	**2014**	**2015**	**2016**	**2017**	**2018**	**2019**	**2020-2024**
Real GDP	1.6	2.2	1.5	2.4	2.2	2.8	2.8	2.6	2.4	2.4
Industrial production	3.3	3.8	2.9	4.1	2.3	3.0	3.1	2.8	2.8	2.6
Consumer spending	2.3	1.5	1.7	2.7	2.9	2.9	2.6	2.5	2.3	2.3
Real disposable personal income	2.5	3.2	-1.4	2.7	3.4	2.5	3.0	2.9	2.6	2.4
Business investment	7.7	9.0	3.0	6.2	3.4	5.2	5.1	4.6	4.1	3.4
Nominal pretax corp. profits	4.0	10.0	2.0	1.7	0.5	4.4	3.1	3.2	3.5	4.4
Total government spending	-3.0	-1.9	-2.9	-0.6	0.5	0.9	NA	NA	NA	NA
Consumer price inflation	3.2	2.1	1.5	1.6	0.2	2.1	2.2	2.3	2.2	2.2
3-month Treasury bill rate	0.05	0.09	0.06	0.03	0.5	1.7	3.4	3.7	3.6	3.5
10-year Treasury bond yield	2.78	1.80	2.35	2.54	2.5	3.2	4.4	4.5	4.5	4.5
Unemployment rate	8.9	8.1	7.4	6.2	5.4	5.0	NA	NA	NA	NA
Housing starts (*millions*)	0.609	0.781	0.925	1.003	1.090	1.270	NA	NA	NA	NA

Source of historical data: U.S. Department of Commerce, U.S. Department of Labor, U.S. Census Bureau, and The Federal Reserve Board.
Source of forecasts: Consensus Forecasts - USA, June 2015.

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INTEREST RATES AND RATES OF RETURN

INTEREST RATES

Interest rate information and rate of return information are presented in Table 1 for a number of different interest rates. U.S. Government securities are considered to have nominal credit risk because they are backed by the full faith and credit of the United States and are extremely liquid. Due to their credit status and the size and liquidity of the government market, yields on U.S. Government securities generally establish the benchmark from which other interest rates and investment returns are determined.

Table 1
Rate of Return and Yield Information
As of June 30, 2015

Asset Group	**06/30/15**
Bank Prime Rate	3.25%
Federal Funds Rate	0.08%
Commercial Paper (3-Month Financial)	0.18%
Treasury (3-Month)	0.01%
Treasury (1-Year)	0.28%
Treasury (20-Year)	2.83%
Treasury (30-Year)	3.11%
Corporate Bonds (Aaa)	4.19%
Corporate Bonds (Baa)	5.18%
IRS Applicable Federal Rate – Long-Term #	2.50%
Investor Capitalization Rate – Weighted Average All Properties	9.42%
Investor Capitalization Rate – Restaurants +	11.70%
PPI Triple Net Lease Partnerships (2014) +	7.70%
PPI Real Estate Partnership Study (2014) +	4.90%
Bond Buyers Index (State & Local Bonds)	3.85%
Conventional Mortgages	4.08%

Source: Federal Reserve Statistical Release Date as of July 6, 2015, except where noted otherwise.
+ **Direct Investments Spectrum, Partnership Profiles, Inc., December 2014.**
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INVESTMENT RETURNS

In addition to the current level of interest rates - risk, liquidity, and maturity are probably the major factors affecting investors' required rate of return on investments in securities and assets. Stocks, Bonds, Bills and Inflation: The Past and the Future by Ibbotson and Sinquefield, a 1982 landmark study, showed how investors have historically been compensated for risk-taking in investments in common stocks. The study included statistical examination of six basic series: common stocks, small capitalization common stocks, long-term corporate bonds, long-term U.S. Government Bonds, U.S. Treasury Bills, and inflation. This analysis computed total rates of return reflecting capital gains and dividends or interest income for each security category.

A 2015 update of the Duff & Phelps / Ibbotson and Sinquefield study determined that investments in small common stock, as represented by the Standard and Poor's 500 Composite Index from 1926 through 2014, have historically provided geometric mean returns of about 5.0 to 6.0 percentage points above the returns on long-term (20-year) U.S. Government Bonds and U.S. Treasury Bills, respectively. In addition, Duff & Phelps compared the historical returns on investments in large New York Stock Exchange (NYSE) stocks in general and in portfolios of small capitalization stocks, those making up the smallest deciles of the New York Stock Exchange. The results of this comparison indicated that returns on micro capitalization stocks have historically been approximately 2.0 percentage points greater than the returns on investments in NYSE large company stocks. The NYSE companies in the low capitalization decile have historically returned about 4.3 percentage points more than the large NYSE companies. The results of the 2014 study and the current level of interest rates indicate that investors may be expecting about a 9.0 percent to 10.0 percent rate of return in common stocks of the largest publicly traded companies; a 10.0 percent to 12.0 percent rate of return for investments in smaller NYSE companies; and a 12.0 percent to 15.0 percent return for the decile of smallest NYSE companies. The historical Ibbotson/Duff & Phelps data is summarized in the following Table 2:

Table 2
Mean Annual Total Returns on Selected Investments: 1926 through 2014
(All Numbers are Percentages)

Investment	Geometric Mean	Arithmetic Mean	Standard Deviation
Large Company Stocks	10.1	12.1	20.1
Small Company Stocks	12.2	16.7	32.1
Long-Term Corporate Bonds	6.1	6.4	8.4
Long-Term Government Bonds	5.7	6.1	10.0
Intermediate-Term Government Bonds	5.3	5.4	5.6
U.S. Treasury Bills	3.5	3.5	3.1
Inflation	2.9	3.0	4.1

Duff & Phelps/Ibbotson Study, 2015 Duff & Phelps Valuation Handbook, Page 2-4.

An alternate method of estimating the expected rate of return on investments in common stock is to sum the current dividend yield and the expected growth rate in corporate profits and dividends.

- The dividend yield for the Standard and Poor's 500 Index was about 1.5 percent as of the Valuation Date.
- Long-term growth in corporate profits and dividends typically track the growth of the general economy. Long-term real GDP growth is expected to be in a range from 2 percent to 3 percent. If the inflation rate is estimated to be 2 percent to 3 percent; the nominal growth rate of GDP would range from 4 percent to 6 percent.
- Data compiled by Yahoo! Finance shows an estimated annual growth rate in market earnings (S&P 500) of about 10 percent per year for the next year.

The preceding data indicates that the estimated return to investors would be approximately 5 percent to 12 percent (nominal growth rate + dividend yield = low end and next five year growth rate + dividend yield = high end). The lower end of this range appears low considering that investors could obtain about 4.7 percent on intermediate grade corporate bonds.