

## Bond Yields Rise as Service Managers Signal Improvement

With two weeks remaining before the next FOMC meeting, most Fed officials seem to support a September pause. At this point, the only data release capable of changing committee member minds is the August CPI report, *on tap for next Wednesday*. That being said, the strength evident in the August ISM service survey will probably spark considerable discussion at the meeting.

The composite ISM Services Index was expected to slip a bit, but actually rose from 52.7 to a six-month high of 54.5. Last week, the ISM Manufacturing Index for August had improved from 46.4 to 47.6, but remained below 50 for the 10th straight month. Recall that any number in this series above 50 indicates *expansion*, while a number below 50 signals *contraction*. Thirteen of 18 service industry groups reported growth last month, in sharp contrast to just two of 18 manufacturing industry groups.

The idea that services are the main driver of economic growth is well established. However, the continued resiliency of the service sector is a bit surprising. U.S. consumer appetite for services was expected to wane as summer ends, but this morning's report suggests unexpected momentum entering the fall months.

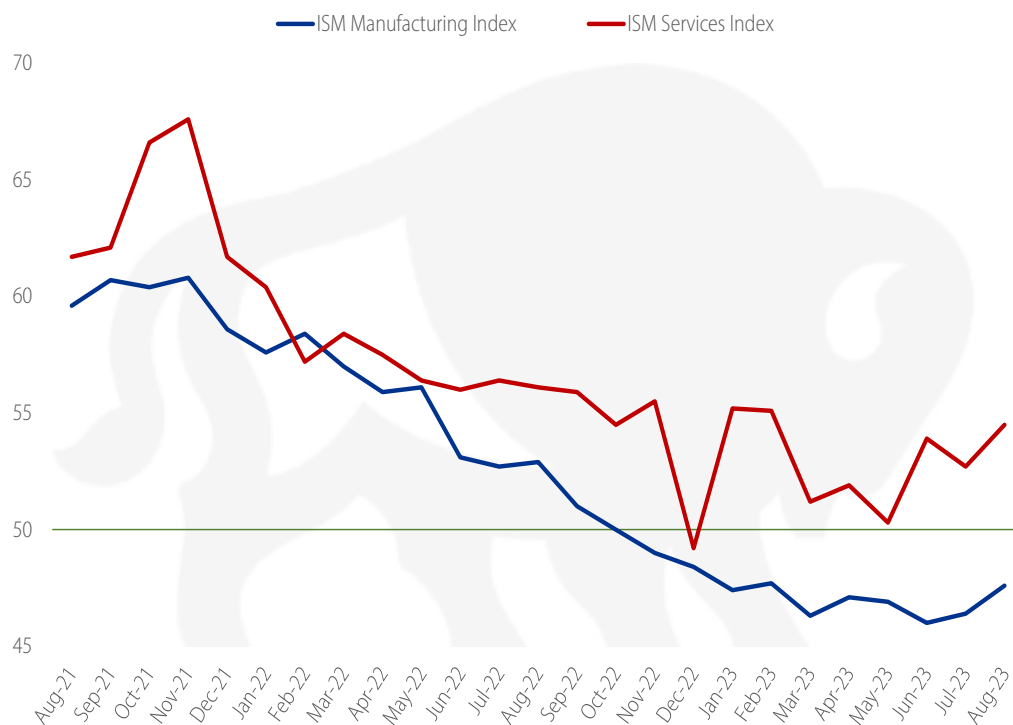
Scott McIntyre, CFA

HilltopSecurities Asset Management  
Senior Portfolio Manager  
Managing Director  
512.481.2009  
scott.mcintyre@hilltopsecurities.com

Greg Warner, CTP

HilltopSecurities Asset Management  
Senior Portfolio Manager  
Managing Director  
512.481.2012  
greg.warner@hilltopsecurities.com

### ISM Purchasing Managers Index



Thirteen of 18 service industry groups reported growth last month, in sharp contrast to just two of 18 manufacturing industry groups.

Source: Institute for Supply Management

Improvement was evident in all of the major subcategories:

- The current production index was already elevated, but increased from 57.1 to 57.3.
- The new orders index signaled that summer spending could extend into the fall, rising from 55.0 to a six-month high of 57.5.
- The employment index climbed from 50.7 to 54.7, a 21-month high, reflecting improvement in the labor force participation rate.
- The prices paid index increased from 56.8 to 58.9, a four-month high, consistent with a rise in energy prices.

*U.S. consumer appetite for services was expected to wane as summer ends, but this morning's report suggests unexpected momentum entering the fall months.*

Bond yields are higher this morning on the better-than-expected data, and although the chances of a September rate hike are still below 10%, the futures market is now signaling a 45% possibility of a quarter point increase in early November, up from 39% before the release.

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If inflation measures hadn't picked up in recent months, investors might welcome signs of economic growth as evidence of the fabled soft-landing. But, with oil prices now at a 15-month high and gasoline prices at their highest level since last October, the inflation battle is clearly not over yet.

## Market Indications as of 11:20 A.M. Central Time

DOW	Down -234 to 34,407 (HIGH: 36,800)
NASDAQ	Down -174 to 13,847 (HIGH: 16,057)
S&P 500	Down -37 to 4,460 (HIGH: 4,797)
1-Yr T-bill	current yield 5.45%; opening yield 5.40%
2-Yr T-note	current yield 5.03%; opening yield 4.95%
3-Yr T-note	current yield 4.74%; opening yield 4.65%
5-Yr T-note	current yield 4.44%; opening yield 4.36%
10-Yr T-note	current yield 4.30%; opening yield 4.25%
30-Yr T-bond	current yield 4.37%; opening yield 4.37%

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