

Economic Watch

US

Houston, April 1, 2013
Economic Analysis

US
Kim Fraser
kim.fraser@bbvacompass.com

Monthly US Outlook: April

Better-than-Expected Data, but is it Sustainable?

Economic indicators have come in better than expected for the first quarter of 2013, but in the large scheme of things we are still far from a comfortable and sustainable pace of recovery. Activity in most sectors has reversed upward after a weak end to 2012, with the labor market leading the way. The unemployment rate dropped to 7.7% in February while nonfarm payrolls increased 236K, the most since November. We have seen above-200K payroll gains in three of the last four months, yet it is still too soon to tell whether these trends can continue without the Federal Reserve's accommodation spurring growth. In the latest FOMC statement and press conference, Ben Bernanke emphasized that they are looking for sustainable job growth, noting that 2-3 months of better reports "...just doesn't cut it" for adjusting policy. Markets have somewhat increased expectations that the Fed will start to scale down asset purchases sooner than previously thought, but it is unlikely that we will see any movement until mid-2013 at the earliest as long as data continue to show signs of a stronger recovery.

Aside from labor market gains, we have also seen solid production and investment trends and resilient consumption even after January's tax hikes. The final estimate for 4Q12 real GDP growth showed an upward revision to 0.4% on a QoQ seasonally-adjusted annualized basis (SAAR), in large part due to a better trade balance and growth in nonresidential structures that had been slightly understated in the prior release. For 2013, we still expect to see annual growth near 1.8% following 2012's 2.2%. Our short-term indicator models suggest slightly above 1.5% for 1Q13, though we expect to see closer to 2.0% in the second half of the year. Of course, government spending will continue to be a drag on growth, but with the continuing resolution helping to offset major impacts in the near-term, we could see a surprise to the upside. The Consolidated and Further Continuing Appropriated Act passed at the end of March allowed for the \$85bn in spending cuts laid out in the sequester and also helped to avoid a government shutdown by funding operations through the end of September.

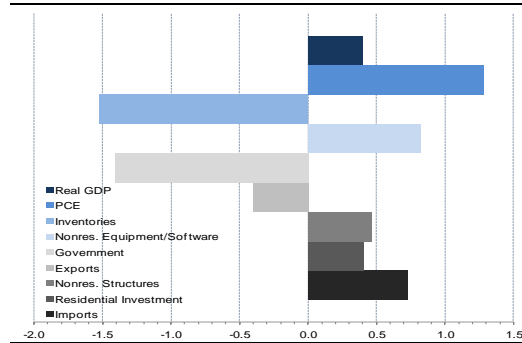
Housing activity has become much more supportive of economic growth as residential demand and construction spending trend upwards. Home prices have jumped significantly throughout the past six months, approaching double-digit annual growth rates, while persistently low mortgage rates have kept housing affordability at record high levels. Existing home sales are showing signs of accelerating improvements, though sales of newer homes appear to be lagging somewhat. New home construction has reached a 5-year high and constrained supply of desirable homes points to increasing demand in the years to come.

Financial markets seem to be the shining star of the economy in 2013 thus far, with positive investor sentiment driving up equity indices to new all-time highs. While corporate spreads don't appear to be narrowing just yet, higher debt issuance suggests that businesses are more confident in expanding in the near future. There hasn't been significant movement in the yield curve but increasing Treasury yields suggest shift away from the "flight-to-safety" mentality towards riskier assets. We have revised up our forecast for the 10-year yield to 2.45% by the end of 2013, nearly 15 basis points higher than last month's estimate. Still, we are not out of the woods yet and may see some temporary volatility if short-term economic news surprise to the downside.

Risks to growth have certainly diminished, but the usual suspects are still on our radar. Inflationary concerns are minimal, with modest gains in oil prices garnering the most attention these days. Renewed volatility in Europe is stemming from Spain and Italy as well as the most recent events in Cyprus, though contagion is more limited now than in prior instances. Domestic fiscal issues are at bay for the time being but will surely intensify as the fiscal year comes to a close.

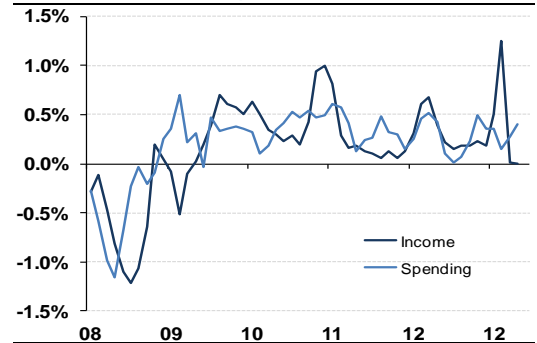
Economic Indicators

Graph 1
Contributions to Real GDP Growth
(4Q12 Final, SAAR Percentage Points)



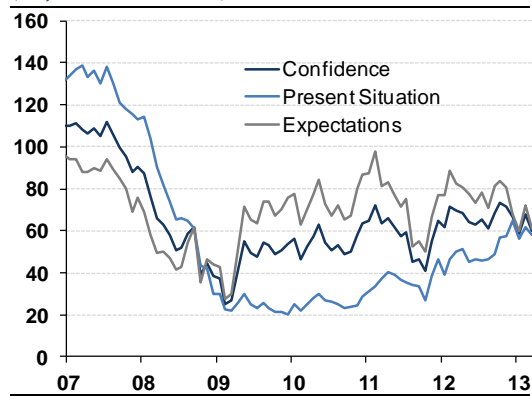
Source: BEA and BBVA Research

Graph 2
Personal Income and Expenditures
(3MMA, MoM % Change)



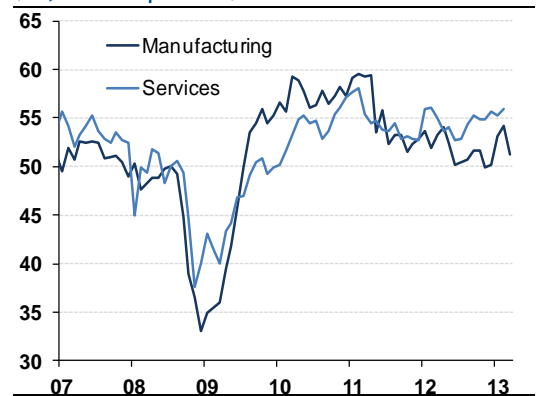
Source: BEA and BBVA Research

Graph 3
Consumer Confidence
(SA, Index 1985=100)



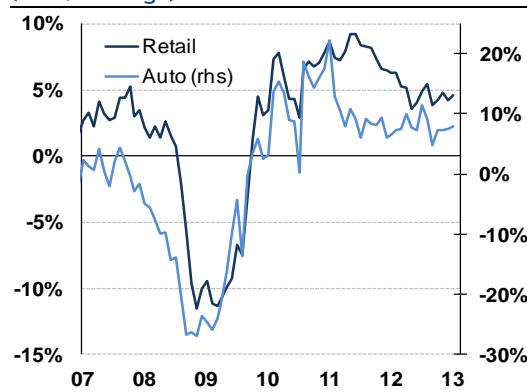
Source: Conference Board and BBVA Research

Graph 4
ISM Indices
(SA, 50+ = Expansion)



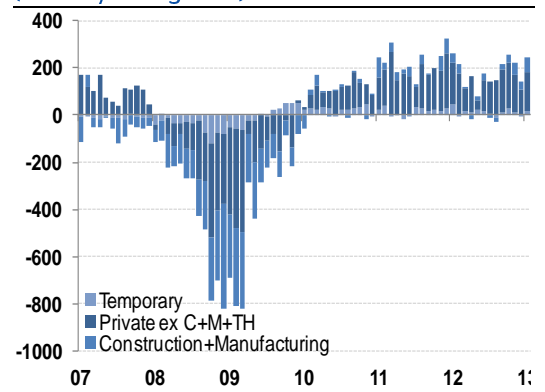
Source: ISM and BBVA Research

Graph 5
Retail and Auto Sales
(YoY % Change)



Source: US Census Bureau and BBVA Research

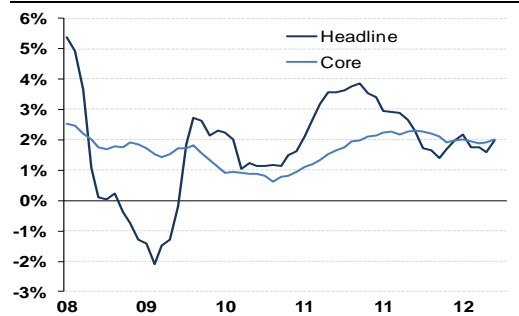
Graph 6
Private Nonfarm Payrolls
(Monthly Change in K)



Source: BLS and BBVA Research

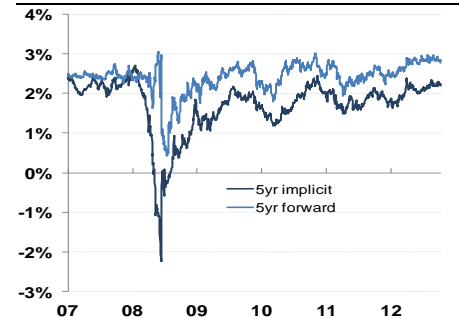
Economic Indicators

Graph 7
Consumer Price Index
(NSA, YoY % Change, 1982-84=100)



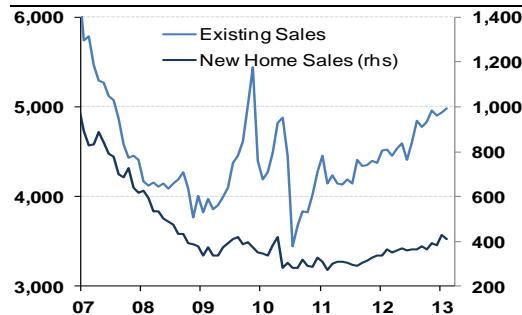
Source: BLS and BBVA Research

Graph 8
Inflation Expectations
(%)



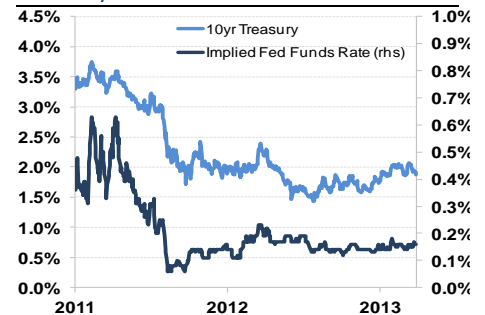
Source: Federal Reserve Board and BBVA Research

Graph 9
New and Existing Home Sales
(Thousands)



Source: US Census Bureau, NAR, and BBVA Research

Graph 10
12-Month Implied Fed Funds Rate & 10-Yr Treasury
(% Yield)



Source: Federal Reserve Board and BBVA Research

Table 1
Forecasts (BOLD=FORECASTS)

	1Q12	2Q12	3Q12	4Q12	2011	2012	2013	2014	2015
Real GDP (% SAAR)	2.0	1.3	3.1	0.4	1.8	2.2	1.8	2.3	2.5
Real GDP (Contribution, pp)									
PCE	1.7	1.1	1.1	1.3	1.8	1.3	1.0	1.2	1.3
Gross Investment	0.8	0.1	0.9	0.2	0.6	1.2	0.8	1.0	1.1
Non Residential	0.7	0.4	-0.2	1.3	0.8	0.8	0.7	0.8	0.9
Residential	0.4	0.2	0.3	0.4	0.0	0.3	0.3	0.2	0.2
Exports	0.6	0.7	0.3	-0.4	0.9	0.5	0.5	1.1	1.3
Imports	-0.5	-0.5	0.1	0.7	-0.8	-0.4	-0.5	-1.1	-1.3
Government	-0.6	-0.1	0.8	-1.4	-0.7	-0.3	-0.1	0.1	0.1
Unemployment Rate (%)	8.3	8.2	8.0	7.8	8.9	8.1	7.4	6.9	6.3
Average Monthly Nonfarm Payroll (K)	262	108	152	209	175	183	155	194	204
CPI (YoY %)	2.8	1.9	1.7	1.9	3.1	2.1	2.1	2.2	2.3
Core CPI (YoY %)	2.2	2.3	2.0	1.9	1.7	2.1	1.9	2.0	2.1
Fiscal Balance (% GDP)	-	-	-	-	-8.7	-7.0	-5.4	-3.8	-2.6
Current Account (bop, % GDP)	-3.5	-3.0	-2.7	-	-3.1	-3.1	-3.0	-3.5	-3.7
Fed Target Rate (% eop)	0.25	0.25	0.25	0.25	0.25	0.25	0.25	0.25	0.50
S&P Case-Shiller Index (YoY %)	-1.19	1.47	3.60	7.35	-4.38	2.78	7.30	5.76	3.85
10-Yr Treasury (% Yield, eop)	2.17	1.62	1.72	1.72	1.98	1.72	2.45	2.73	3.39
U.S. Dollar / Euro (eop)	1.32	1.25	1.29	1.31	1.31	1.31	1.32	1.30	1.35
Brent Oil Prices (dps, average)	118.4	108.5	109.7	110.3	111.3	111.7	109.0	112.9	119.0

Source: BBVA Research

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