

Economic Analysis

2Q14 GDP Expands at Fastest Pace since 4Q11

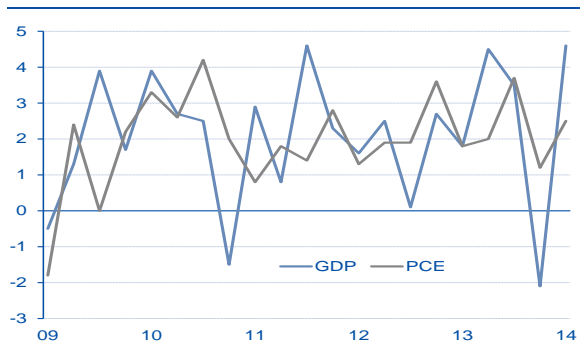
Kim Fraser Chase

The final estimate for real GDP growth in 2Q14 was revised up to 4.6% QoQ SAAR from the initial 4.0% estimate released a few months ago. This marks the strongest pace for quarterly growth since 4Q11 and is enough to offset the 2.1% contraction seen in 1Q14. Upward revisions to exports and residential investment were significant drivers of the higher growth rate, with both making almost a full recovery from the losses incurred in the first quarter. Personal consumption growth was unchanged at 2.5%, and we expect that this healthy pace will continue throughout the second half of the year. Overall, this stronger-than-expected final figure puts slight upward pressure on our annual forecast; however, we are maintaining our projection for 2.0% growth in 2014. Economic activity in 3Q14 thus far has not been overwhelmingly positive, and we expect that GDP growth for the quarter may seem somewhat disappointing after 2Q's robust final estimate. In general, we expect to see growth average just above 2.0% for the third and fourth quarters. Our expectation for real GDP growth in 2015 remains unchanged at 2.5%.

August's Strength in New Home Sales Offsets Gloomy Existing Home Data

Existing home sales declined in August for the first time since March, setting off worries that another weak quarter is in store for residential investment. Constrained supply has certainly been a key factor in holding back sales of existing homes, particularly given that the number of distressed (yet more affordable) properties have declined significantly throughout the past year. Elevated home prices and increasing mortgage rates have hurt affordability, which has dropped to the lowest level of the recovery period thus far. However, the fate of the housing recovery does not rest solely in the hands of the existing home market. New home sales in August were surprisingly upbeat, rising 18.0% from July to 504K and marking the highest level of the long recovery period thus far. This is certainly positive news to at least partially offset the discouraging demand for existing homes. However, new homes account for just over 9% of the housing market and cannot fully lead the residential recovery. We do expect that housing sales (both existing and new) will continue to increase gradually throughout the coming years, but it has become clearer that housing activity will not be a driving force of GDP growth at least for the near term.

Graph 1
Real GDP and PCE Growth
(QoQ SAAR % Change)



Source: Bureau of Economic Analysis & BBVA Research

Graph 2
New and Existing Home Sales
(SAAR, Thousands)



Source: NAR, Census, & BBVA Research

Week Ahead

Personal Income and Outlays (August, Monday 8:30 ET)

Forecast: 0.3%, 0.2%

Consensus: 0.3%, 0.4%

Previous: 0.2%, -0.1%

Personal income and outlays are expected to have a better showing in August as consumers loosen their purse strings for another busy shopping season. Data in July surprised to the downside, with personal income growth decelerating and consumption declining for the first time since January. However, we do expect to see a healthy rebound in August, particularly for personal spending as the back-to-school shopping season gets underway. While we do not expect the month to be extremely overwhelming, we should at least see some positive indications of healthy consumer activity during the month.

S&P Case-Shiller Home Price Index (July, Tuesday 9:00 ET)

Forecast: 7.8%

Consensus: 7.4%

Previous: 8.1%

The S&P Case-Shiller HPI is expected to increase slightly in July, but annual growth is likely to decelerate for the eighth consecutive month. According to the composite 20-city index, home prices declined in both May and June as supply in the existing home market became a bit less strained. However, demand is still sluggish and the lack of distressed properties on the market has been keeping away more first-time homebuyers, at least for the time being. Overall, the home price index has recovered about halfway from the crisis and is expected to continue moving gradually towards the pre-recession peak throughout the next few years.

Nonfarm Payrolls and Unemployment Rate (September, Friday 8:30 ET)

Forecast: 203K, 6.1%

Consensus: 215K, 6.1%

Previous: 142K, 6.1%

Nonfarm payroll growth was surprisingly slow in August but is expected to pick back up in September. Average monthly job growth set a recovery record between February and July, with six straight months of above 200K gains. August's slowdown primarily reflected a lack of hiring in manufacturing, which we expect will turn around in the coming months. However, hiring in the construction sector may struggle given the disappointing housing market data as of late. Overall, labor force flows are still heavily influencing the rapid decline in the unemployment rate, yet we expect that this trend will slow down in the coming months.

International Trade (August, Friday 8:30 ET)

Forecast: -\$41.0B

Consensus: -\$41.0B

Previous: -\$40.6B

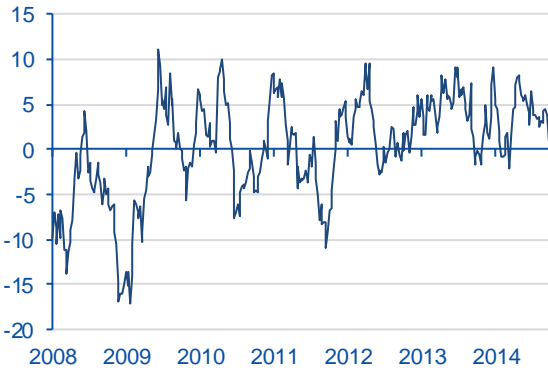
The international trade balance improved significantly in June and July but is expected to widen slightly in August. Export growth accelerated in July and is likely to do the same in August, although not enough to offset stronger import growth. Increased domestic demand for the back-to-school shopping season on top of a stronger dollar should boost total imports for the month. Furthermore, we may see a reversal in the petroleum trade gap, which has narrowed throughout the past five months but only changed slightly from June to July. Either way, we do not expect to see a major shift in the trade balance for August.

Market Impact

This week's economic calendar is full of important market-moving variables. Markets will be primarily looking toward Friday's employment report with the hopes that job growth improved from August. Economic data will continue to warrant market reaction as it relates to the Fed's next steps in their monetary policy strategy.

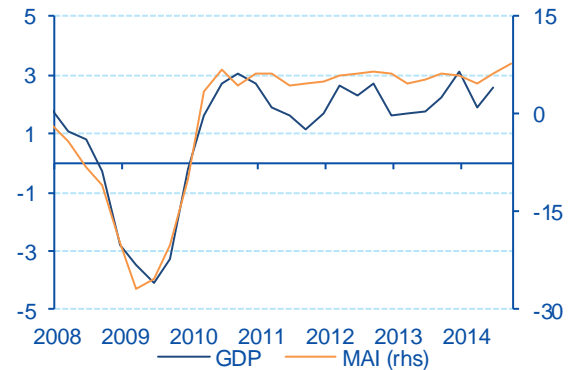
Economic Trends

Graph 3
BBVA US Weekly Activity Index (3 month % change)



Source: BBVA Research

Graph 4
BBVA US Monthly Activity Index & Real GDP (4Q % change)



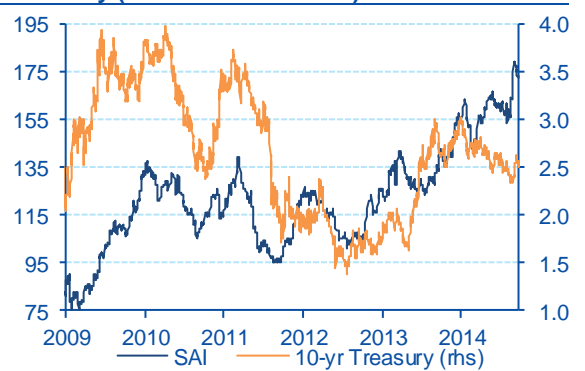
Source: BBVA Research & BEA

Graph 5
BBVA US Surprise Inflation Index (Index 2009=100)



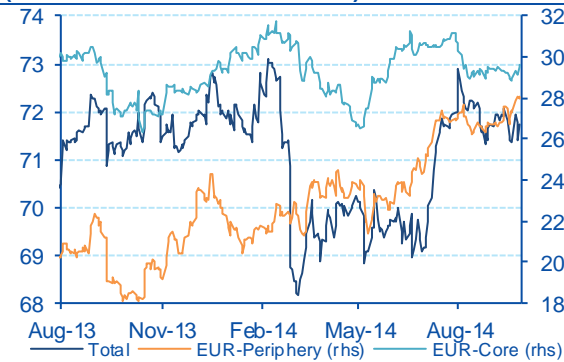
Source: BBVA Research

Graph 6
BBVA US Surprise Activity Index & 10-yr Treasury (Index 2009=100 & %)



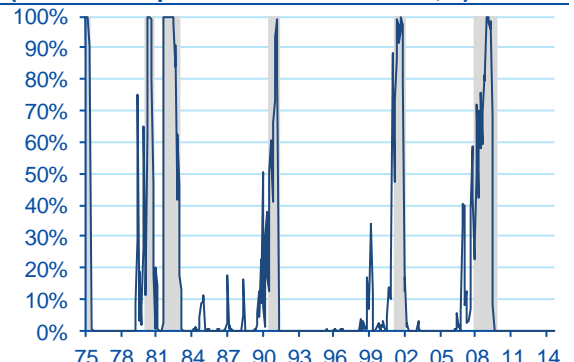
Source: Bloomberg & BBVA Research

Graph 7
Equity Spillover Impact on US (% Real Return Co-Movements)



Source: BBVA Research

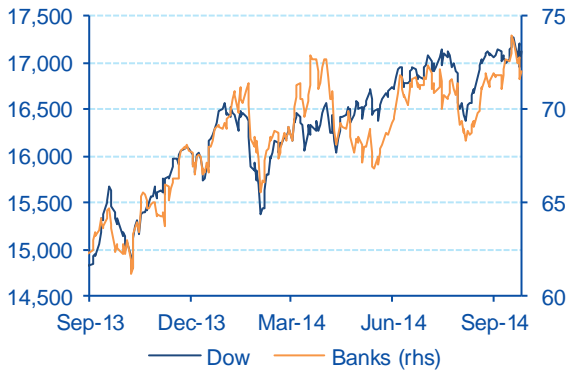
Graph 8
BBVA US Recession Probability Model (Recession episodes in shaded areas, %)



Source: BBVA Research

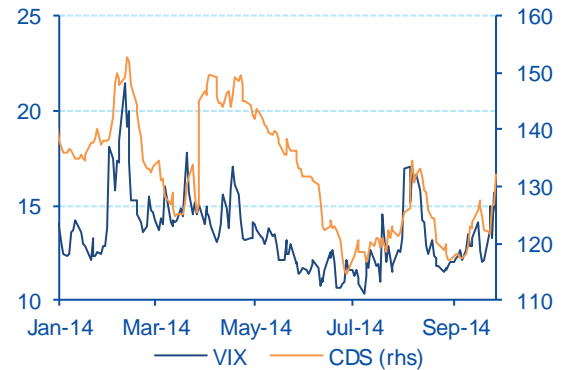
Financial Markets

Graph 9
Stocks
(Index, KBW)



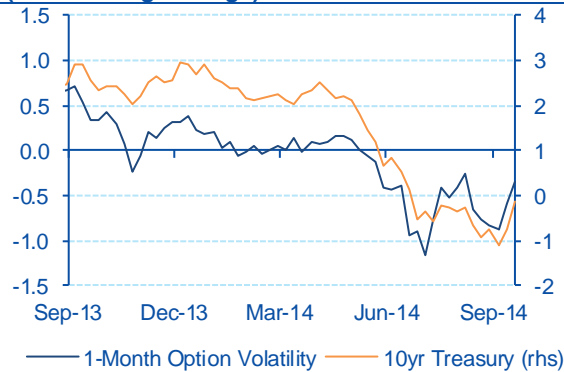
Source: Bloomberg & BBVA Research

Graph 10
Volatility & High-Volatility CDS
(Indices)



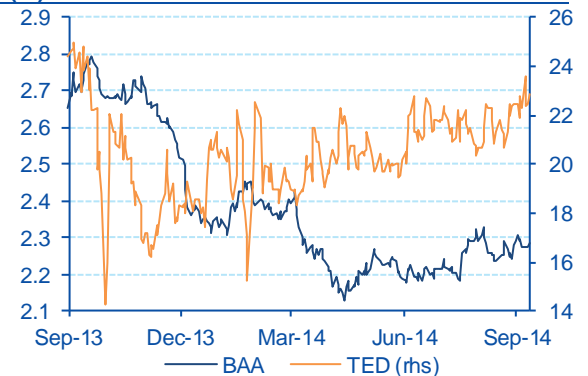
Source: Bloomberg & BBVA Research

Graph 11
Option Volatility & Real Treasury
(52-week avg. change)



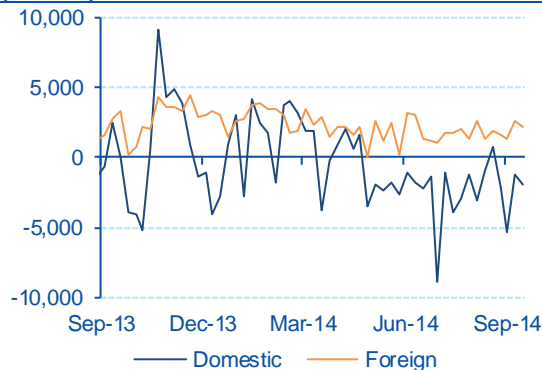
Source: Haver Analytics & BBVA Research

Graph 12
TED & BAA Spreads
(%)



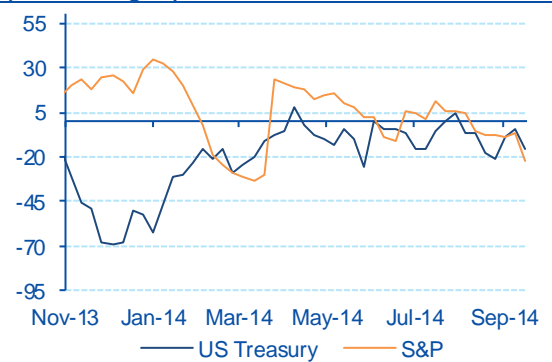
Source: Bloomberg & BBVA Research

Graph 13
Long-Term Mutual Fund Flows
(US\$Mn)



Source: Haver Analytics & BBVA Research

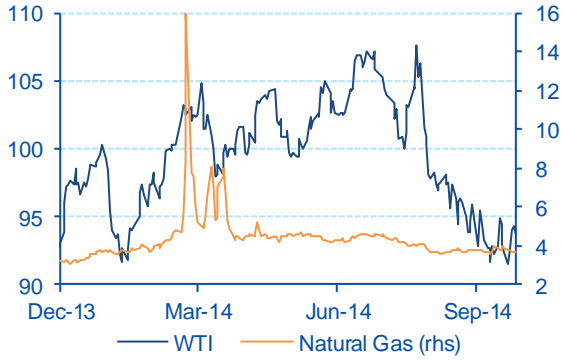
Graph 14
Total Reportable Short & Long Positions
(Short-Long, K)



Source: Haver Analytics & BBVA Research

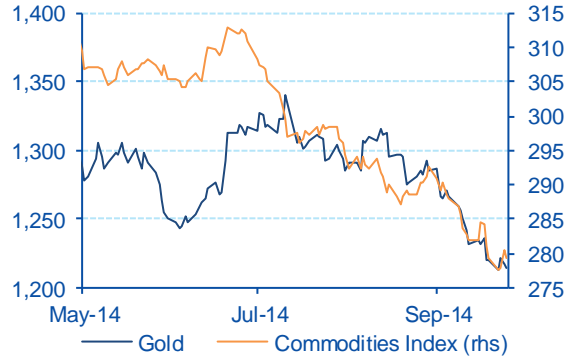
Financial Markets

Graph 15
Commodities
(Dpb & DpMMBtu)



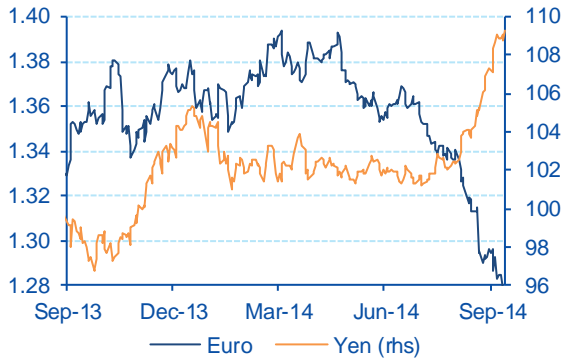
Source: Bloomberg & BBVA Research

Graph 16
Gold & Commodities
(US\$ & Index)



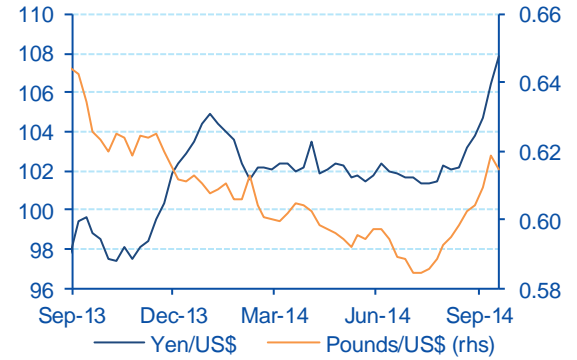
Source: Haver Analytics & BBVA Research

Graph 17
Currencies
(Dpe & Ypd)



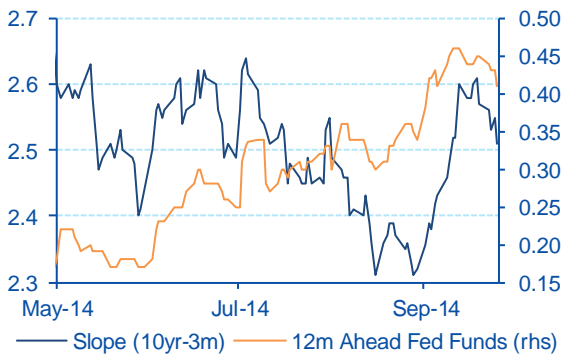
Source: Bloomberg & BBVA Research

Graph 18
6-Month Forward Exchange Rates
(Yen & Pound / US\$)



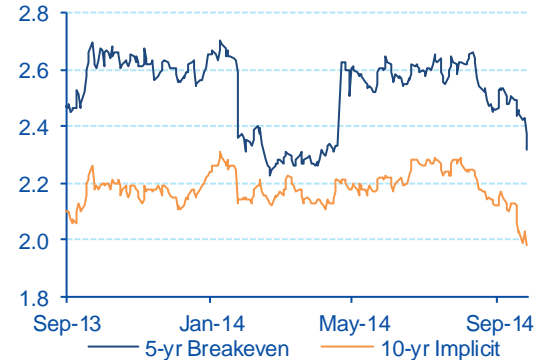
Source: Haver Analytics & BBVA Research

Graph 19
Fed Futures & Yield Curve Slope
(% & 10year-3month)



Source: Haver Analytics & BBVA Research

Graph 20
Inflation Expectations
(%)



Source: Bloomberg & BBVA Research

Interest Rates

Table 1
Key Interest Rates (%)

	Last	Week ago	4-Weeks ago	Year ago
Prime Rate	3.25	3.25	3.25	3.25
Credit Card (variable)	14.86	14.86	14.86	14.10
New Auto (36-months)	2.93	2.93	2.93	2.50
Heloc Loan 30K	4.82	4.81	4.97	5.19
5/1 ARM *	3.08	3.06	2.97	2.90
15-year Fixed Mortgage *	3.36	3.37	3.25	3.23
30-year Fixed Mortgage *	4.20	4.23	4.10	3.99
Money Market	0.42	0.42	0.39	0.42
2-year CD	0.89	0.87	0.85	0.80

*Freddie Mac National Mortgage Homeowner Commitment US
Source: Bloomberg & BBVA Research

Table 2
Key Interest Rates (%)

	Last	Week ago	4-Weeks ago	Year ago
1M Fed	0.09	0.09	0.07	0.08
3M Libor	0.23	0.23	0.23	0.25
6M Libor	0.33	0.33	0.32	0.37
12M Libor	0.58	0.58	0.55	0.63
2yr Sw ap	0.82	0.81	0.71	0.47
5yr Sw ap	1.95	1.98	1.78	1.58
10Yr Sw ap	2.66	2.71	2.50	2.81
30yr Sw ap	3.20	3.28	3.07	3.69
30day CP	0.11	0.12	0.11	0.12
60day CP	0.12	0.11	0.11	0.15
90day CP	0.13	0.13	0.13	0.13

Source: Bloomberg & BBVA Research

Quote of the Week

Loretta J. Mester, Federal Reserve Bank of Cleveland President and CEO
The Economic Outlook, Monetary Policy, and Getting Back to Normal
24 September 2014

“Even though the Committee has emphasized that policy is contingent on the state of the economy, in my view, the “considerable time” part of the guidance tends to focus the public’s attention on a calendar-time for liftoff rather than on the changes in economic conditions that will help determine changes in appropriate policy.”

Economic Calendar

Date	Event	Period	Forecast	Survey	Previous
29-Sep	US Personal Income MoM SA	AUG	0.30	0.30	0.20
29-Sep	US Personal Consumption Expenditures Nominal Dollars MoM SA	AUG	0.20	0.40	-0.10
29-Sep	US Pending Home Sales Index MoM SA	AUG	0.30	-0.40	3.32
29-Sep	Dallas Fed Manufacturing Outlook Level Of General Business Activity	SEP	5.50	10.50	7.10
30-Sep	S&P/Case-Shiller Composite-20 City Home Price Index SA MOM % Change	JUL	0.40	-0.10	-0.20
30-Sep	S&P/Case-Shiller Composite-20 City Home Price Index YoY	JUL	7.80	7.40	8.07
30-Sep	MNI Chicago Business Barometer (sa)	SEP	63.90	62.00	64.30
30-Sep	Conference Board Consumer Confidence SA 1985=100	SEP	93.00	92.45	92.40
1-Oct	ADP National Employment Report SA Private Nonfarm Level Change	SEP	200.00	207.50	204.30
1-Oct	US Auto Sales Total Annualized SA	SEP	17.20	16.80	17.45
1-Oct	ISM Manufacturing PMI SA	SEP	59.70	58.30	59.00
1-Oct	Census Bureau US Construction Spending MoM SA	AUG	0.70	0.50	1.80
2-Oct	US Initial Jobless Claims SA	SEP 27	297.00	296.50	293.00
2-Oct	US Continuing Jobless Claims SA	SEP 20	2465.00	2430.00	2439.00
2-Oct	NEW YORK PURCHASING MANAGER Current Business Conditions SA	SEP	57.30	--	57.10
2-Oct	US Manufacturers New Orders Total MoM SA	AUG	-5.10	-9.30	10.50
3-Oct	US Trade Balance Balance Of Payments SA	AUG	-41.00	-40.95	-40.55
3-Oct	US Employees on Nonfarm Payrolls Total MoM Net Change SA	SEP	203.00	215.00	142.00
3-Oct	US Employees on Nonfarm Payrolls Total Private MoM Net Change SA	SEP	200.00	210.00	134.00
3-Oct	US Employees on Nonfarm Payrolls Manufacturing Industry Monthly Net Change SA	SEP	10.00	13.00	0.00
3-Oct	US Average Hourly Earnings All Employees Total Private Monthly Percentage Change	SEP	0.10	0.20	0.20
3-Oct	US Average Weekly Hours All Employees Total Private SA	SEP	34.50	34.50	34.50
3-Oct	ISM Non-Manufacturing NMI NSA	SEP	60.10	58.50	59.60

Forecasts

	2011	2012	2013	2014	2015	2016	2017
Real GDP (% SAAR)	1.8	2.8	1.9	2.0	2.5	2.8	2.8
CPI (YoY %)	3.1	2.1	1.5	1.9	2.2	2.3	2.4
CPI Core (YoY %)	1.7	2.1	1.8	2.0	2.1	2.3	2.4
Unemployment Rate (%)	8.9	8.1	7.4	6.3	5.9	5.8	5.5
Fed Target Rate (eop, %)	0.25	0.25	0.25	0.25	0.50	1.50	2.50
10Yr Treasury (eop, % Yield)	1.98	1.72	2.90	3.00	3.50	3.75	4.00
US Dollar/ Euro (eop)	1.31	1.31	1.37	1.31	1.29	1.36	1.36

DISCLAIMER

This document was prepared by Banco Bilbao Vizcaya Argentaria's (BBVA) BBVA Research U.S. on behalf of itself and its affiliated companies (each BBVA Group Company) for distribution in the United States and the rest of the world and is provided for information purposes only. Within the US, BBVA operates primarily through its subsidiary Compass Bank. The information, opinions, estimates and forecasts contained herein refer to the specific date and are subject to changes without notice due to market fluctuations. The information, opinions, estimates and forecasts contained in this document have been gathered or obtained from public sources, believed to be correct by the Company concerning their accuracy, completeness, and/or correctness. This document is not an offer to sell or a solicitation to acquire or dispose of an interest in securities.