

Economic Outlook

US Monthly Update

December 7, 2012

Meeting Details

Topic: US Monthly Economic Outlook

Date: Friday, December 7, 2012

Time: 10:00 am, Central Standard Time (Chicago, GMT-06:00)

Meeting Number / Access Code: 716 273 042

Meeting Password: bbva

To join the online meeting:

<https://bbvacompass.webex.com/bbvacompass/j.php?ED=188893947&UID=1407861422&PW=NNjAyYTIhOTQ0&RT=MiM3>

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Call-in toll-free number (US/Canada): 1-866-469-3239

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Global call-in numbers:

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Bottom Line

Economic Activity

- Impact from Sandy implies lower 4Q12 GDP growth; will reverse in 1H13

Monetary Policy

- No room for comfort yet
- Replacing OT with Treasuries purchases

Financial Markets

- Becoming anxious on the fiscal cliff

Interest Rates

- Still value on the curve: End of OT vs. political surprises

Risks

- Tilted to the downside: fiscal cliff, deleverage, Euro crisis, EMs & geopolitical

Economic Activity

Data	Last	3m ago	6m ago	12 m ago
ISM	49.5	49.6	53.5	52.2
ISM nonmanufacturing	54.7	53.7	53.7	52.6
Capacity utilization	77.8	79.2	79.0	77.6
Industrial production (yoy % chg)	1.7	4.2	5.0	4.2
Capital goods new orders (yoy % chg)	-7.1	-7.8	2.9	15.4
Unemployment rate (%)	7.9	8.3	8.1	8.9
Nonfarm payroll (Thou)	171	181	68	112
Auto sales (Million)	15.5	14.5	13.9	13.5
Real disposable income (yoy % chg)	1.2	1.5	0.7	0.7
Real personal spending (yoy % chg)	1.3	1.8	1.8	2.3
Retail sales ex autos & gas (yoy % chg)	2.9	4.3	5.0	7.0
Consumer confidence (Index)	73.7	61.3	64.4	55.2
Housing starts (yoy % chg)	41.9	18.6	35.3	16.0
Home prices (CS/SP, yoy % chg)	3.0	0.6	-2.6	-3.6

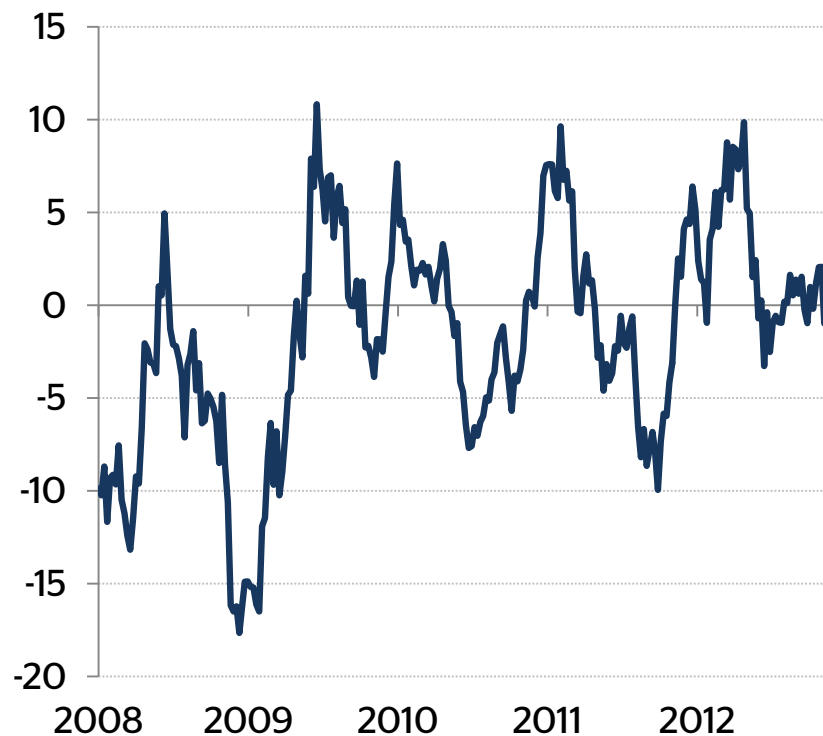
- Production and investment slow
- Slight advance in labor markets
- Modest uptick in personal spending and income growth
- Healthier housing market

Baseline Scenario

Economic activity stable at around 2%. The temporary shock from Sandy will drag down 4Q12 GDP growth

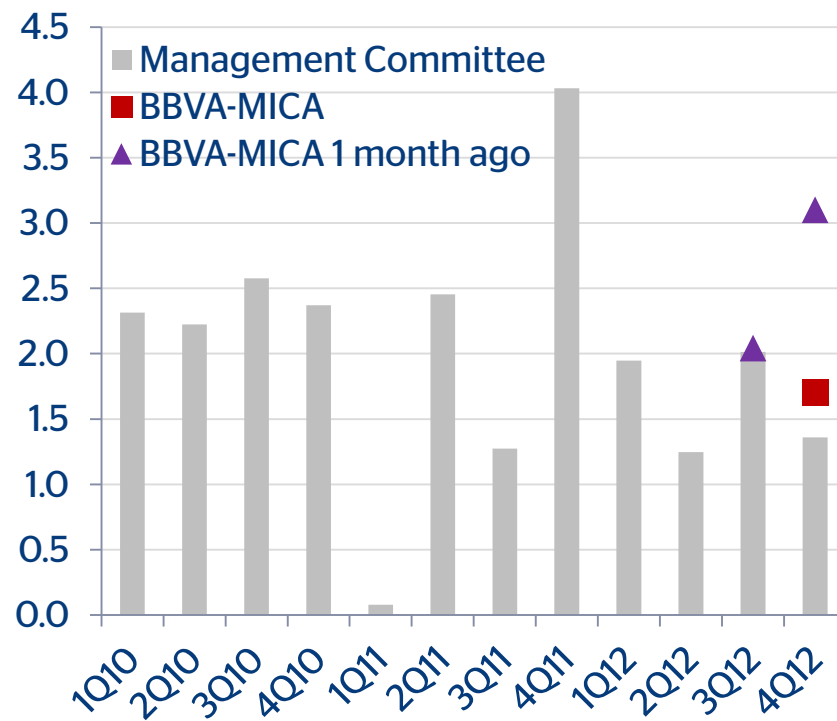
BBVA US Weekly Activity Index

3m % change



Real GDP Growth

QoQ SAAR, %

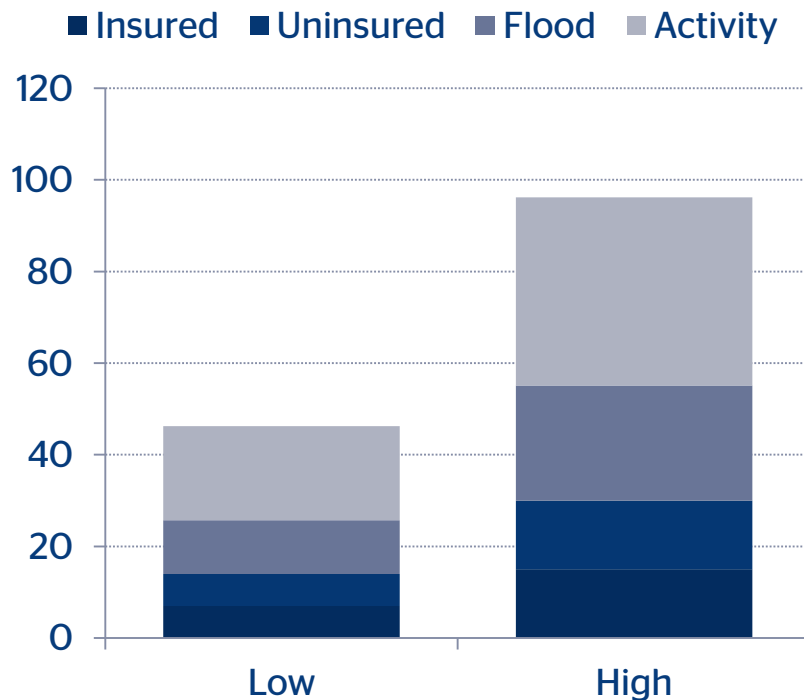


Hurricane Sandy

Reconstruction activity in 1H13 is likely to offset most of the negative effects

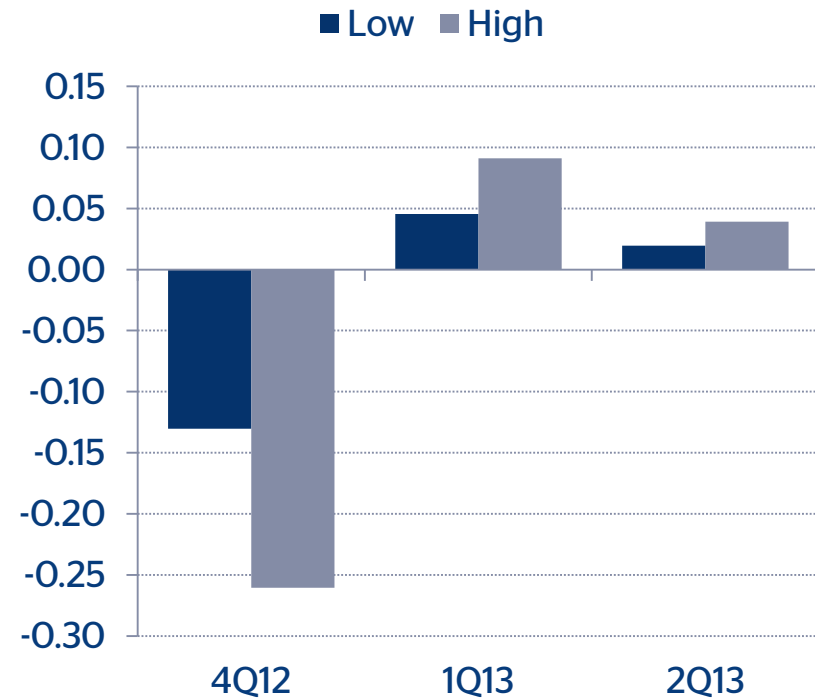
Hurricane Sandy Estimated Costs

Property losses and economic activity, US\$bn



Hurricane Sandy Net Impact on GDP growth

Percentage points



2012 Election Implications

- No major changes to break *status quo*

- Narrow margin of victory, strong partisanship, small and shrinking number of centrists, failure of both parties to obtain a sufficient majority in the Senate to pass legislation
- Divisions in the electorate reflecting the economy and demographics will resonate in the daily debate: strong divisions by race, age, gender, social views, and the role of the government

- However, the electorate is demanding action and cooperation

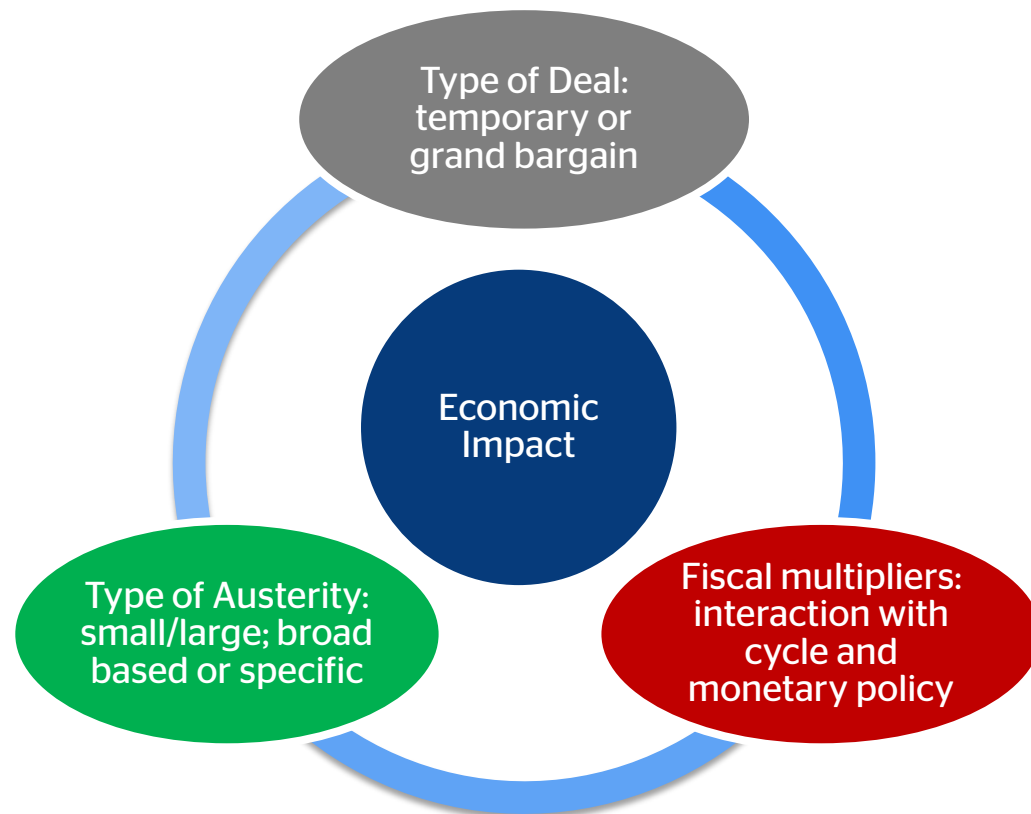
- How does the GOP interpret defeat: Bad policies or a bad candidate?
- Is the President more willing to move to the center in his 2nd term?

- A long list of priorities... which are unlikely to be tackled swiftly

- Fiscal cliff, debt ceiling, tax reform, entitlements, immigration, energy, the environment, healthcare and financial system

Fiscal Cliff

The outcome of the political negotiations and the potential economic impact are highly uncertain



•Type of deal

- A pre-12/31 deal. Ideal but unlikely
- A multi-step deal: the most likely outcome at this stage
- Full cliff: undesirable but probable. This opens the door to a retroactive deal which can itself be temporary or permanent

•Type of austerity

- Main differences given by ideological positions, not economic rationale
- Uncertainty and long-term fiscal sustainability resolved?

•Multipliers:

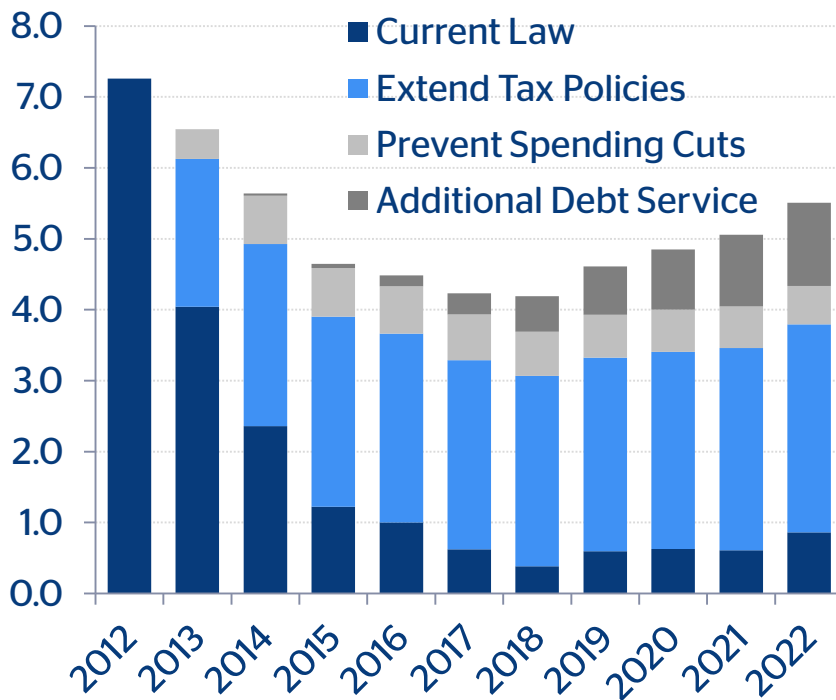
- How much has been priced in?
- Are multipliers greater at the Zero Lower Bound?
- Timeline of the impact

Fiscal Cliff

Regardless of the options, Congress needs to reach on a balanced agreement: Too much austerity vs. fiscal sustainability

Fiscal Deficit

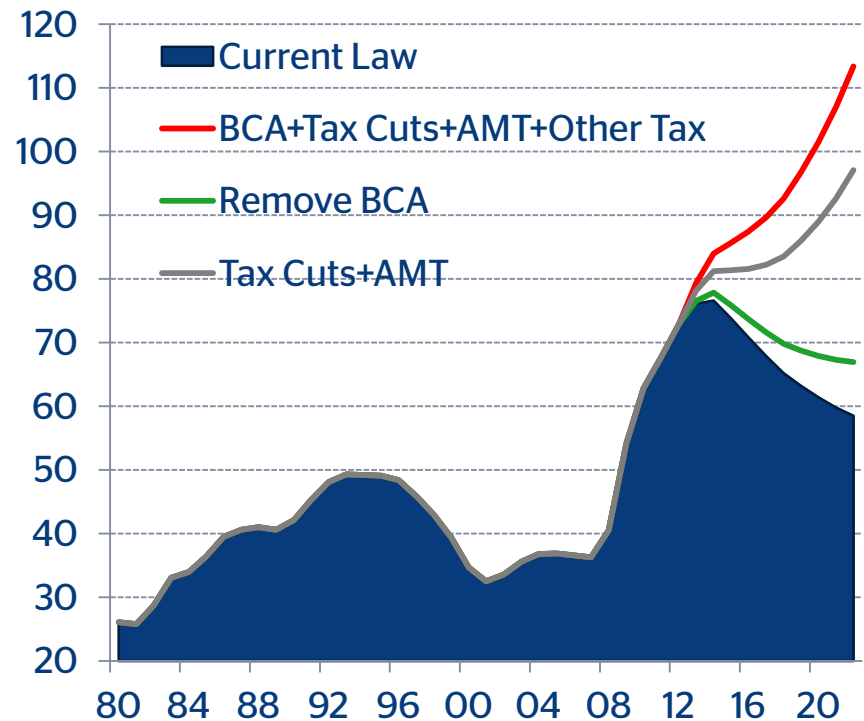
% of GDP



Source: BBVA Research, & Haver

Public Debt held by the Public

% of GDP

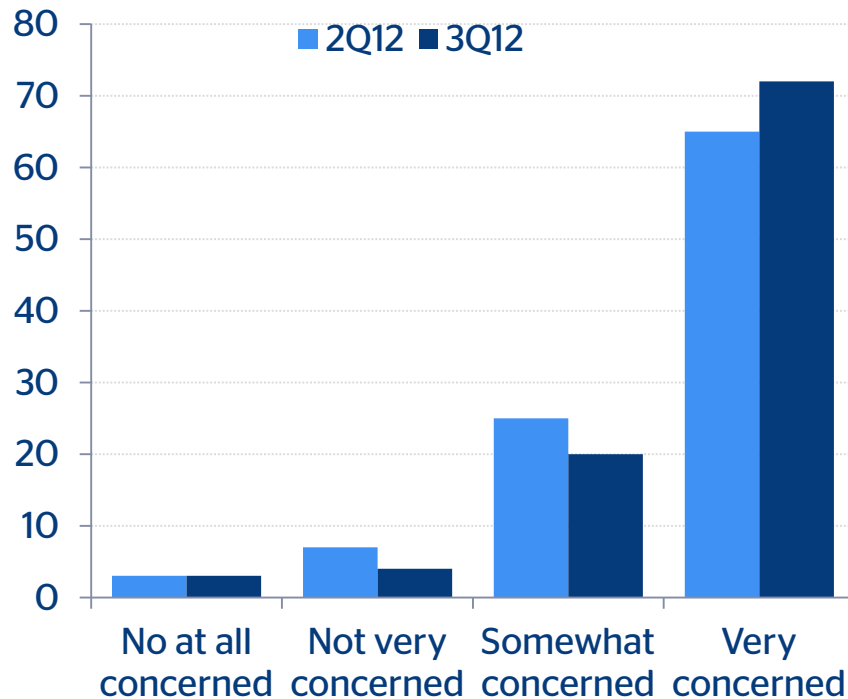


Fiscal Cliff

A “bad” outcome could be highly detrimental to the weak economic recovery

Small Business Survey on the Fiscal Cliff

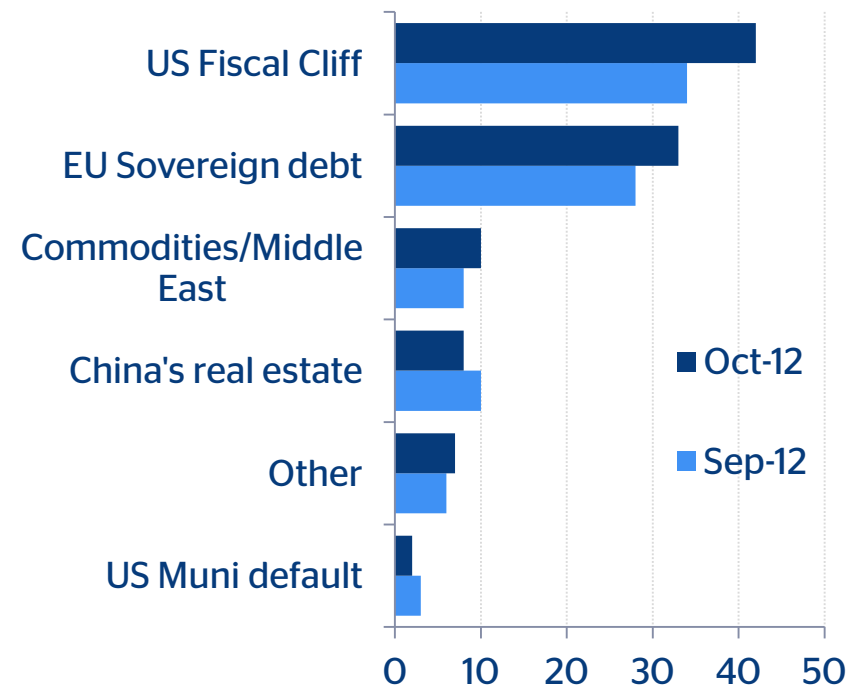
% of responses



Source: US Chamber of Commerce

Top Concerns among US Investors

% of responses



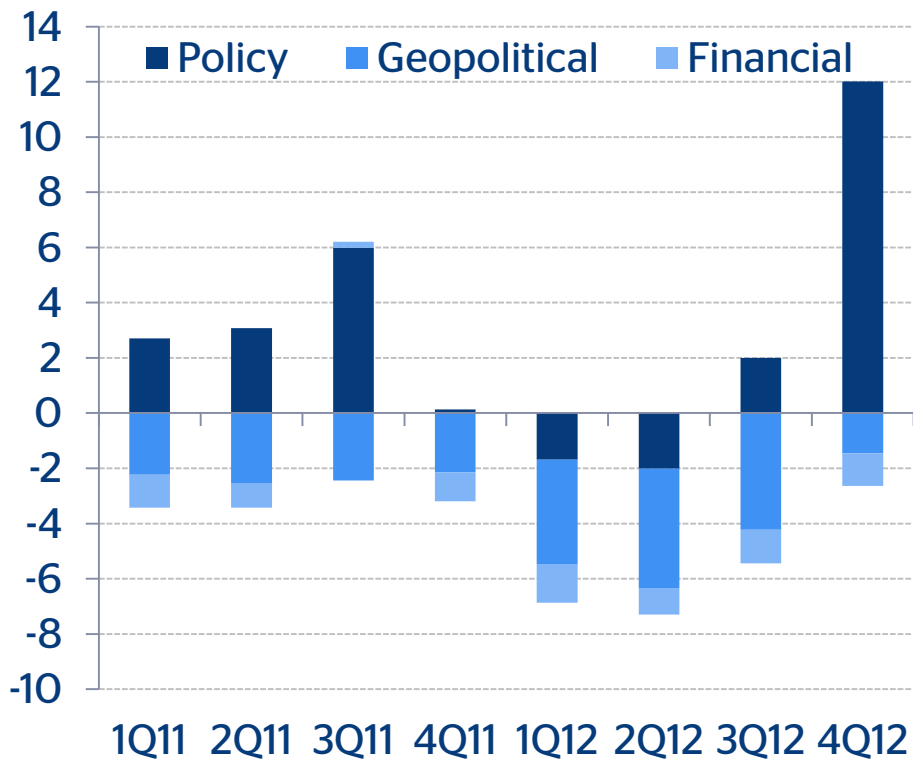
Source: Merrill Lynch/BofA

Policy Uncertainty

At a minimum, failure to reach compromise over the Fiscal Cliff will likely ripple through markets resulting in weak economic growth in 1H13

BBVA Policy Uncertainty Index

Contribution to Uncertainty Index



Policy Uncertainty

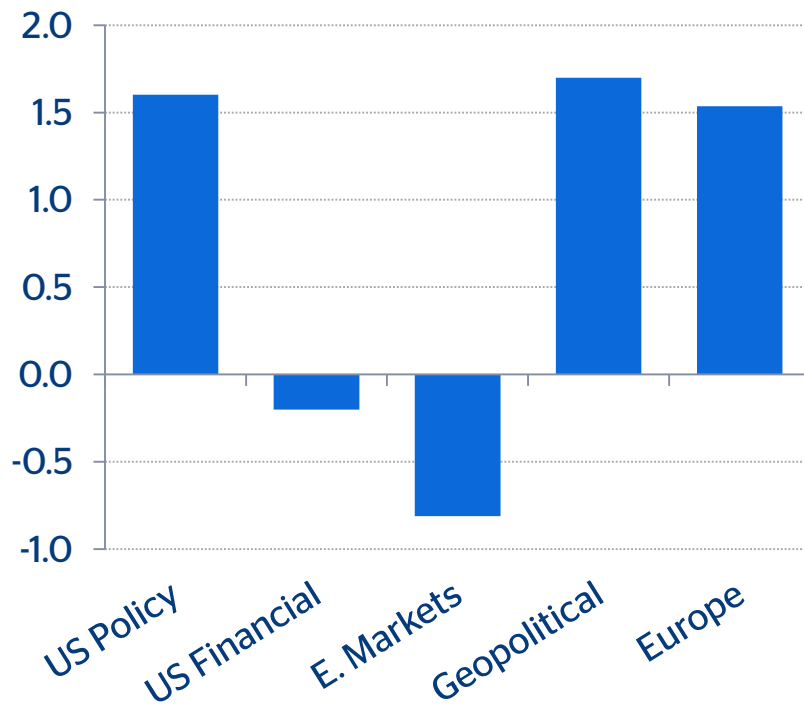
- Policy uncertainty is dominating consumer and corporate expectations
- Underlying the policy uncertainty is the on going “fiscal cliff” negotiations which encompass a combination of expiring tax policies and previously legislated sequestration (Budget Control Act)
- Although geopolitical uncertainty remains below historical levels, the index has increased from 2Q12 lows, adding to aggregate uncertainty risk

Composite Risk Index

Under current conditions, the major risks are related to U.S. policy uncertainty, geopolitical volatility, and Europe.

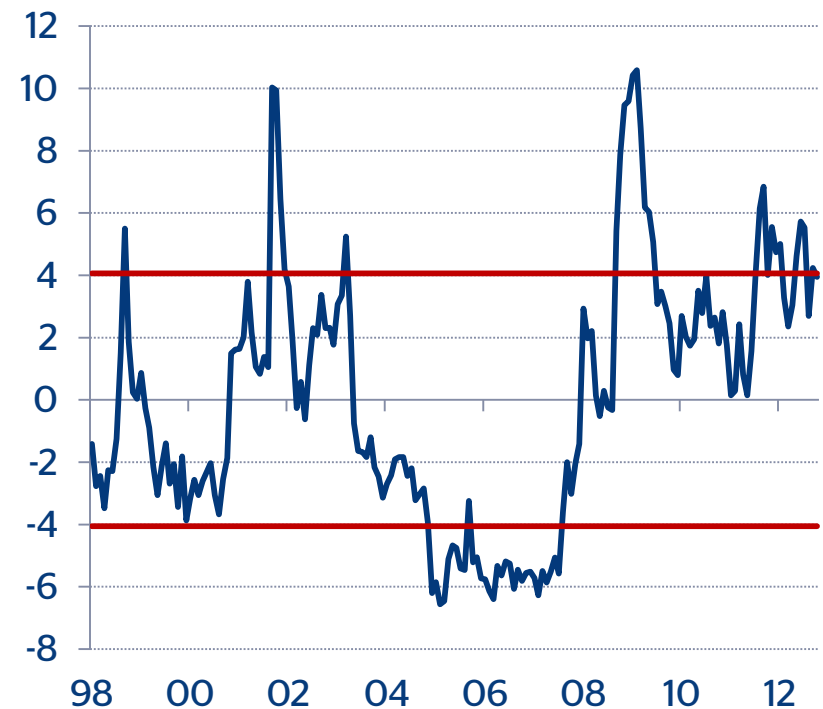
Risk Components

Last relative to historical average



Risk Index

Average=0; sd=+/- 4



Baseline Scenario

No changes to our scenario other than long-term interest rates

	2011	2012	2013	2014
GDP %	1.7	2.1	1.8	2.3
CPI %	3.2	2.0	2.1	2.4
Core %	1.7	2.1	1.9	2.0
Fed %, eop	0.25	0.25	0.25	0.25
10YTN %, eop	1.89	1.76	2.35	2.80
Euro epd, eop	1.30	1.23	1.31	1.31

Meeting Feedback

We would appreciate any feedback you have for us.

<http://www.surveymonkey.com/s/6D3S7NV>

Thank you for participating!

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