

Economic Outlook

US Monthly Update

January 9, 2013

Meeting Details

Topic: US Monthly Economic Outlook

Date: Wednesday, January 9, 2013

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

Meeting Number / Access Code: 717 030 607

Meeting Password: bbva

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Fiscal Cliff

The American Taxpayer Relief Act of 2012 was passed by Congress on January 1, 2013, and was signed into law by President Obama the next day

Spending Provisions

- The budget sequestration created by the Budget Control Act of 2011 is delayed by two months, to give time for further negotiations on deficit reduction
- The \$24 billion cost would be offset by a provision allowing 401(k) accounts to be rolled over into Roth IRA plans, requiring taxes to be paid on the assets, as well as a requirement for unspecified cuts of \$4 billion for the remainder of FY2013 and \$8 billion in FY 2014
- Federal unemployment benefits are extended for a year without a budget offset elsewhere
- The Medicare doc fix is extended for one year
- A pay freeze for members of Congress is extended, but a general pay freeze for government workers is not
- Some portions of the farm bill that had expired in September are extended for nine months, but without changes supported by dairy farmers and legislators

Fiscal Cliff

Revenue Provisions

- The top marginal tax rate on income of 39.6% is retained for individuals with taxable income of over \$400K/\$450K. Tax rates for those with incomes below those amounts revert from higher rates imposed under the expiration provision of the Bush tax cuts, back down to their year 2012 levels
- The top marginal tax rate on capital gains of 20% is retained for those in the \$400K/\$450K upper income bracket, but the tax rates for those below that bracket revert from higher rates imposed under the expiration provision of the Bush tax cuts, back down to their year 2012 levels of 15%
- The top marginal tax rate on dividends of 39.6% is lowered to 20% for those in the \$400K/\$450K upper income bracket, but the tax rates for those below that bracket revert from higher rates imposed under the expiration provision of the Bush tax cuts, back down to their year 2012 levels of 15%
- A phase-out of tax deductions and credits for incomes over \$250K for individuals and \$300K for couples is reinstated
- Estate taxes are set at 40% of the value above \$5.25M, indexed for inflation, an increase from the 2012 rate of 35% of the value over \$512M.
- Changes to the Alternative Minimum Tax to permanently index it to inflation and thus to avoid the annual "patch" that was previously required to prevent it from impacting middle-class families
- The two-year old cut to payroll taxes expires
- Some tax credits for poorer families are extended for five years, including ones for college tuition and an expansion of the Earned Income Tax Credit
- A number of corporate tax breaks are extended, including the "active financing" tax exemption for major corporations, a rum tax supporting Puerto Rico and Virgin Islands rum industry, a tax benefit for NASCAR racetrack owners, tax credits for two- and three-wheeled electric vehicles and hiring of individuals who are members of a Native American tribe

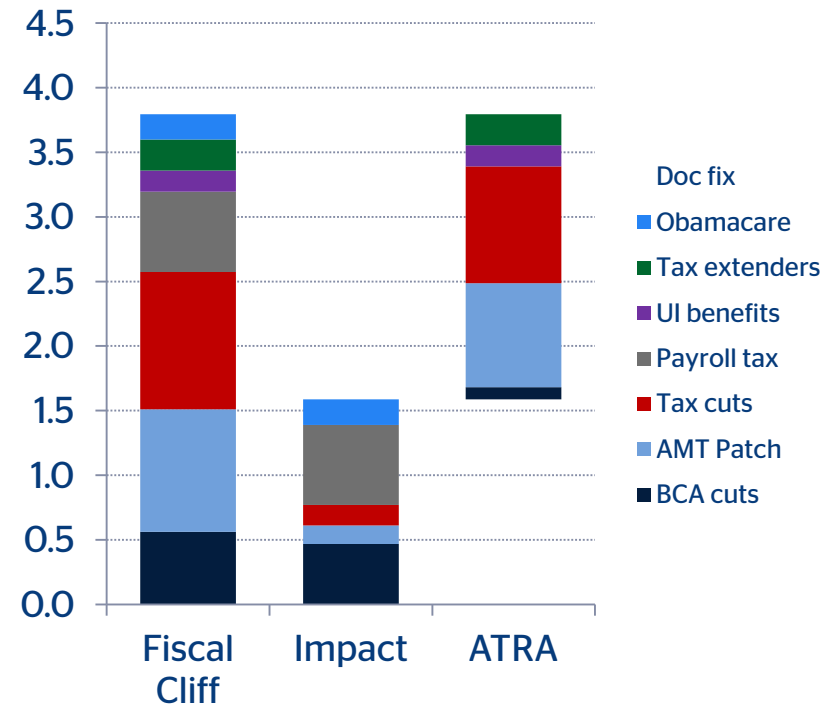
Fiscal Cliff

Lawmakers met our expectations: Another kicked can

- The deal represents a wasted opportunity to improve fiscal conditions
- Positive: Avoids an abrupt economic impact; increases revenues; extension of the sequester and doc fix with offsetting provisions; and leaves open the option to discuss a more meaningful agreement
- Negative: No entitlement reform; no pro-growth policy measures; no debt sustainability triggers; missed opportunity for a grand-bargain

American Taxpayer Relief Act

% of GDP, CY 2013



Source: BBVA Research & Haver

Baseline Scenario

No changes to our scenario

	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	1.78	2.35	2.80
Euro epd, eop	1.30	1.32	1.31	1.31

Economic Activity

Data	Last	3m ago	6m ago	12 m ago
ISM	50.7	51.5	49.7	53.1
ISM nonmanufacturing	56.1	55.1	52.1	53.0
Capacity utilization	78.4	78.3	78.9	77.7
Industrial production (yoy % chg)	2.5	2.9	4.6	4.1
Capital goods new orders (yoy % chg)	1.1	-4.3	2.2	3.2
Unemployment rate (%)	7.8	7.8	8.2	8.5
Nonfarm payroll (Thou)	155	132	45	223
Auto sales (Million)	15.3	14.9	14.3	13.5
Real disposable income (yoy % chg)	2.5	1.5	1.3	0.3
Real personal spending (yoy % chg)	2.1	1.9	1.9	1.9
Retail sales ex autos & gas (yoy % chg)	3.7	3.6	4.7	6.0
Consumer confidence (Index)	65.1	68.4	62.7	64.8
Housing starts (yoy % chg)	21.6	29.1	28.1	29.9
Home prices (CS/SP, yoy % chg)	4.3	1.2	-1.8	-3.6

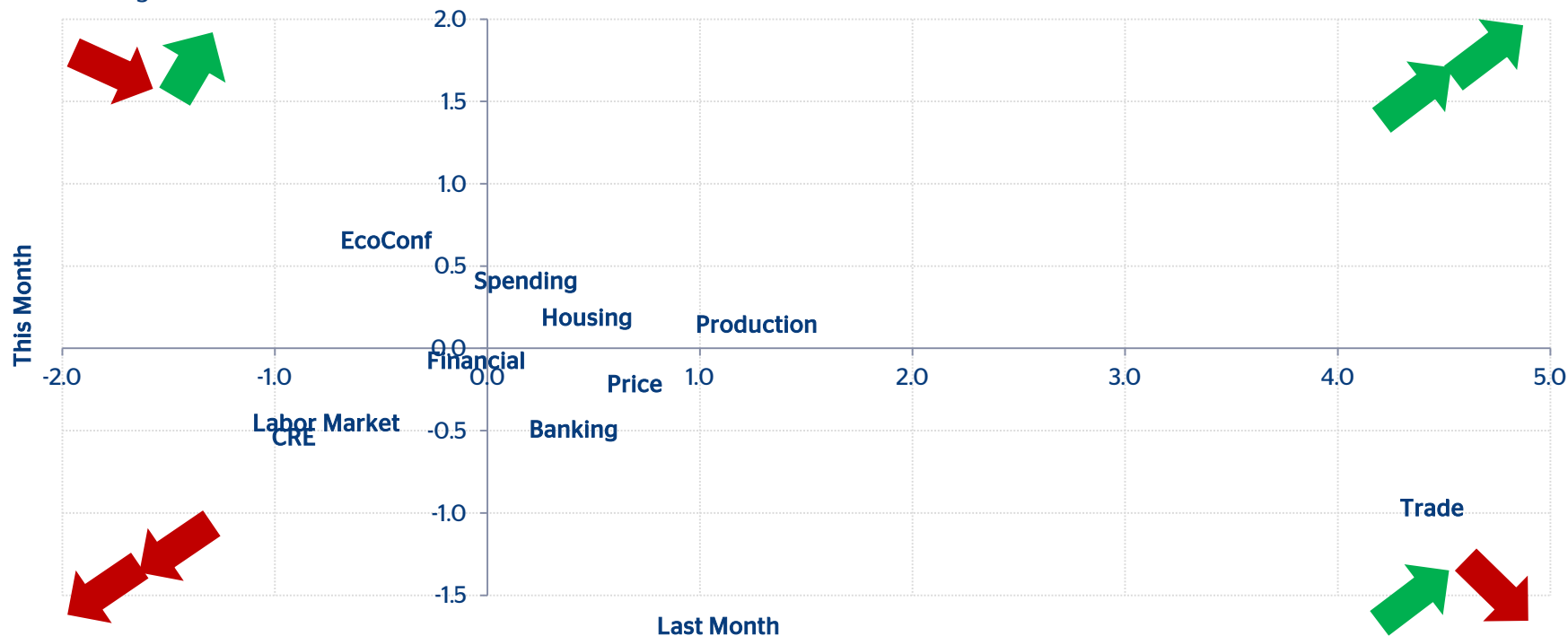
- Stable production and investment
- Moderate improvement in job growth
- Stronger spending and income growth
- Ongoing housing recovery

Economic Activity

Despite lingering fiscal cliff uncertainty in December, business confidence and production appeared to be on the rise. However, January's data could tell another story.

BBVA Monthly Activity Index Trends

MoM Change

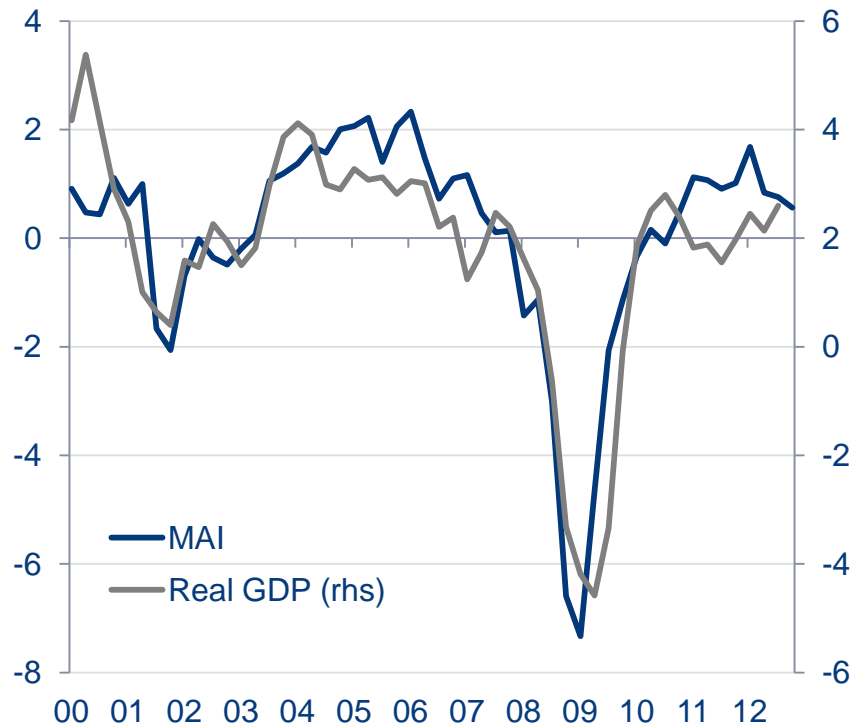


Economic Activity

Economic data from early in 4Q and the surprising jump in 3Q GDP growth suggest a slightly slower pace to close out 2012.

BBVA US Monthly Activity Index

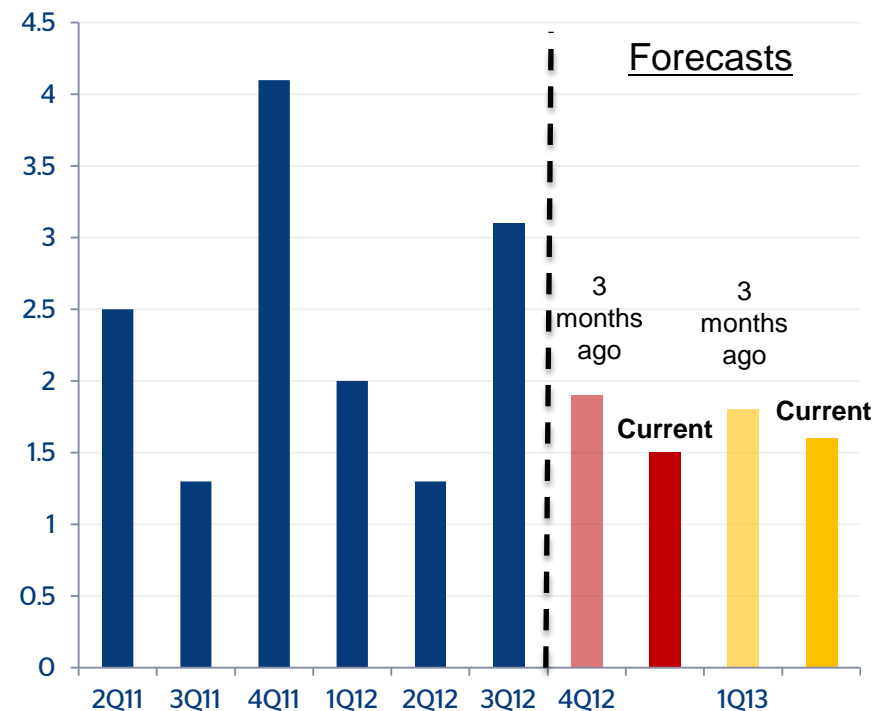
4Q % Change



Source: BEA & BBVA Research

Real GDP Growth

QoQ SAAR, %



Small Business Optimism

Looming uncertainties are still a burden, and it may be a while before the outlook improves

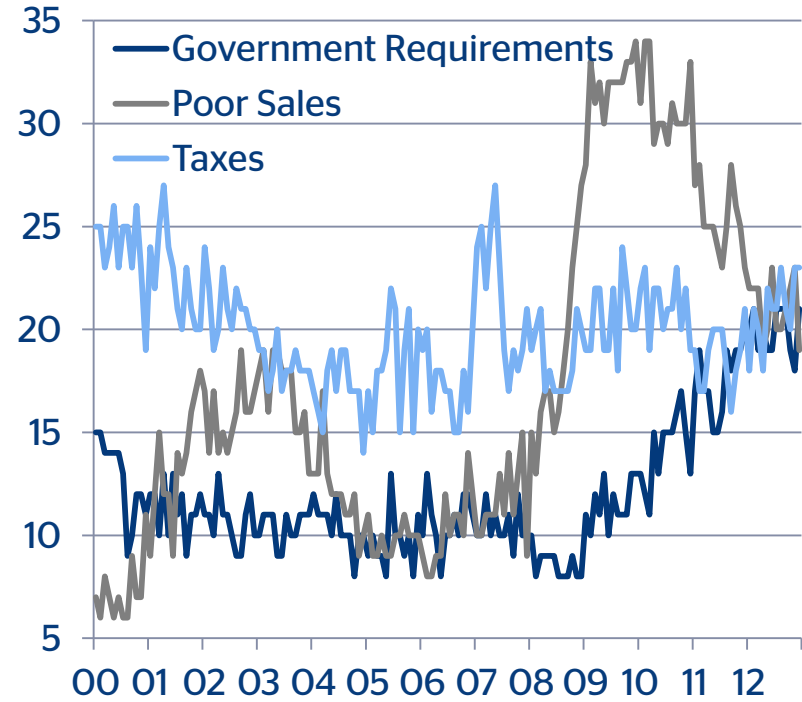
Small Business Optimism & Job Conditions

SA Index and %



Single Most Important Problem

% Reporting



Note: While there is no standard definition of a "small business," the typical NFIB member employs 10 people and reports gross sales of about \$500,000 a year

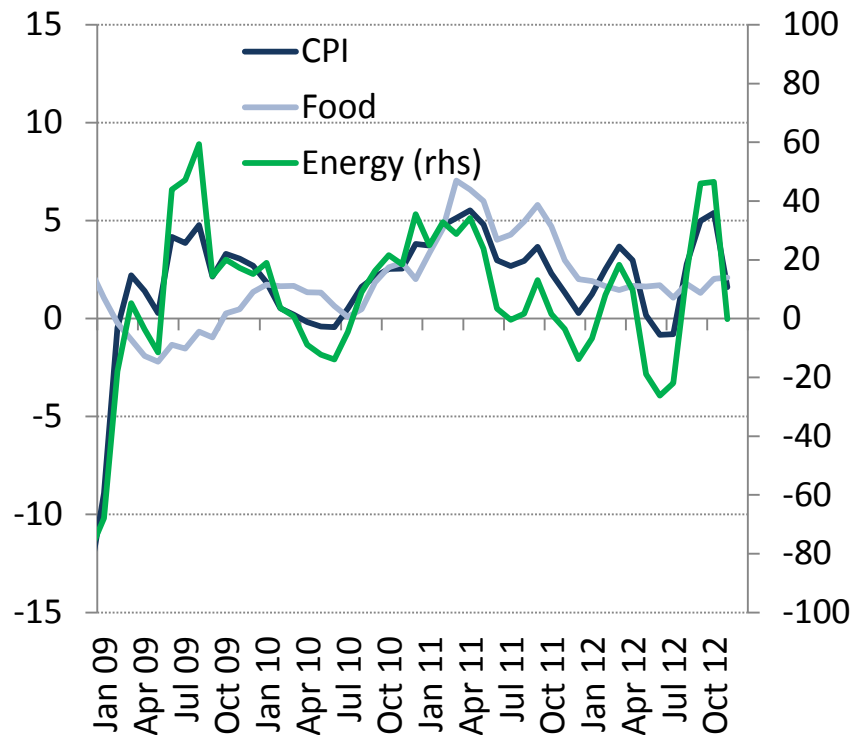
Source: National Federation of Independent Business & BBVA Research

Inflation

Energy prices are helping to offset some pressures on shelter and food prices

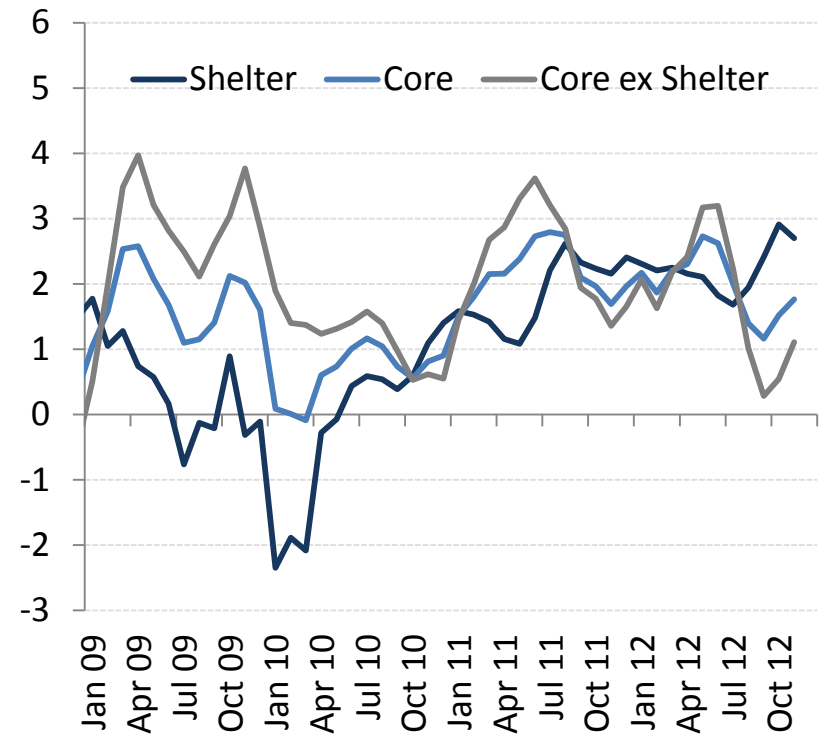
CPI Prices

3m % change, annualized



Core Prices

3m % change, annualized



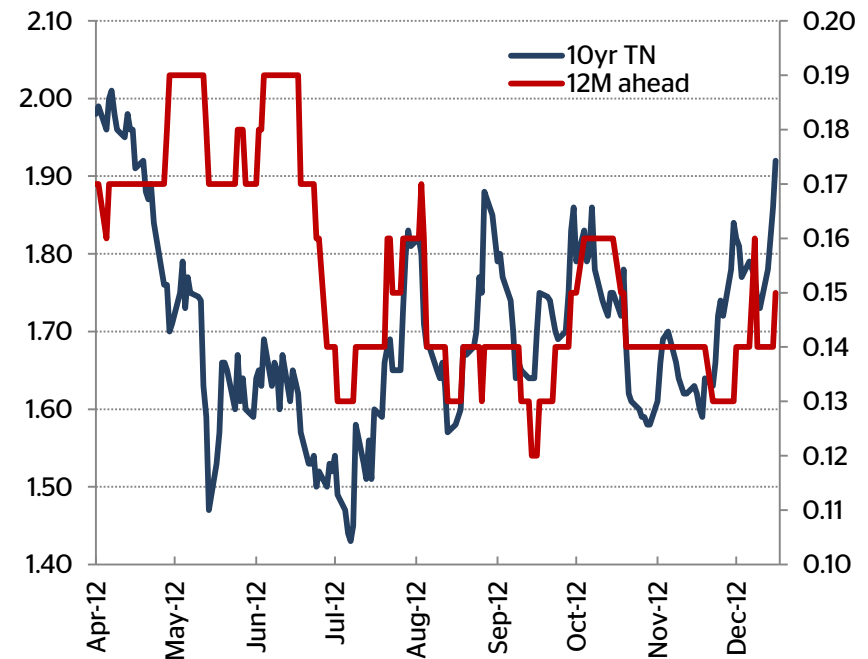
Monetary Policy

Minutes of the Federal Open Market Committee December 11-12, 2012

- Growing differences within the FOMC reflecting uncertainty on the economic outlook and the need to extend QE for much longer
- “A few members expressed the view that ongoing asset purchases would likely be warranted until about the end of 2013, while a few others emphasized the need for considerable policy accommodation but did not state a specific time frame or total for purchases. Several others thought that it would probably be appropriate to slow or to stop purchases well before the end of 2013, citing concerns about financial stability or the size of the balance sheet.”

10YTN & Fed funds

US\$ billions



Source: BBVA Research / Haver

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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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