

Economic Outlook

US Monthly Update

February 7, 2013

Meeting Details

Topic: US Monthly Economic Outlook

Date: Thursday, February 7, 2013

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

Meeting Number / Access Code: 717 648 151

Meeting Password: bbva

To join the online meeting:

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Bottom Line

- Improved financial market conditions
 - Resilience in domestic economic indicators
 - Moderate impact of hurricane Sandy
 - Certainty on monetary policy/FOMC statement & minutes
 - Fiscal deal at year-end 2012
 - Stronger-than-expected data in EM
- Can it last?
 - Still weak fundamentals in Europe
 - Elevated US Policy uncertainty
- Key Risks:
 - Negative surprises on the policy side
 - Sharp movement in interest rates for the wrong reason

Economic Activity

Data	Last	3m ago	6m ago	12 m ago
ISM	53.1	51.7	50.5	53.7
ISM nonmanufacturing	55.7	55.2	52.7	52.7
Capacity utilization	78.8	78.4	78.8	78.3
Industrial production (yoy % chg)	2.2	3.0	4.5	3.8
Capital goods new orders (yoy % chg)	-4.6	-7.8	-1.7	8.0
Unemployment rate (%)	7.9	7.9	8.2	8.3
Nonfarm payroll (Thou)	157	160	153	311
Auto sales (Million)	15.2	14.2	14.1	13.9
Real disposable income (yoy % chg)	5.6	1.7	1.3	0.0
Real personal spending (yoy % chg)	2.2	1.9	2.0	1.7
Retail sales ex autos & gas (yoy % chg)	4.4	4.5	3.3	5.6
Consumer confidence (Index)	58.6	73.1	65.4	61.1
Housing starts (yoy % chg)	36.9	30.3	22.6	29.3
Home prices (CS/SP, yoy % chg)	5.5	2.0	-0.5	-3.9

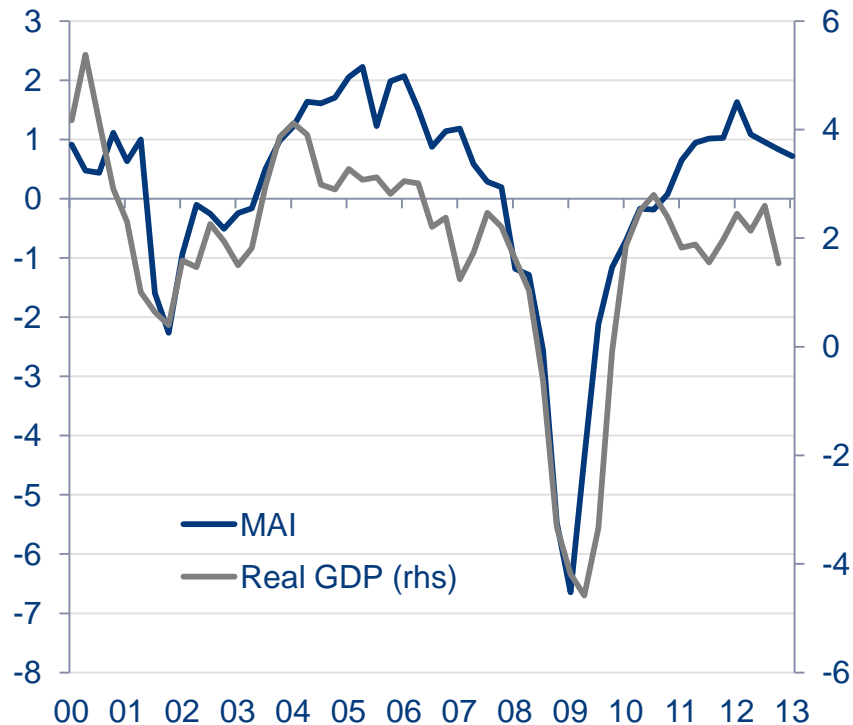
- Positive surprises in production
- Ongoing improvement in job growth
- Resilient spending and income growth
- Ongoing housing recovery

Economic Activity

Our short-term indicators suggest subpar growth for 4Q12 and 1Q13

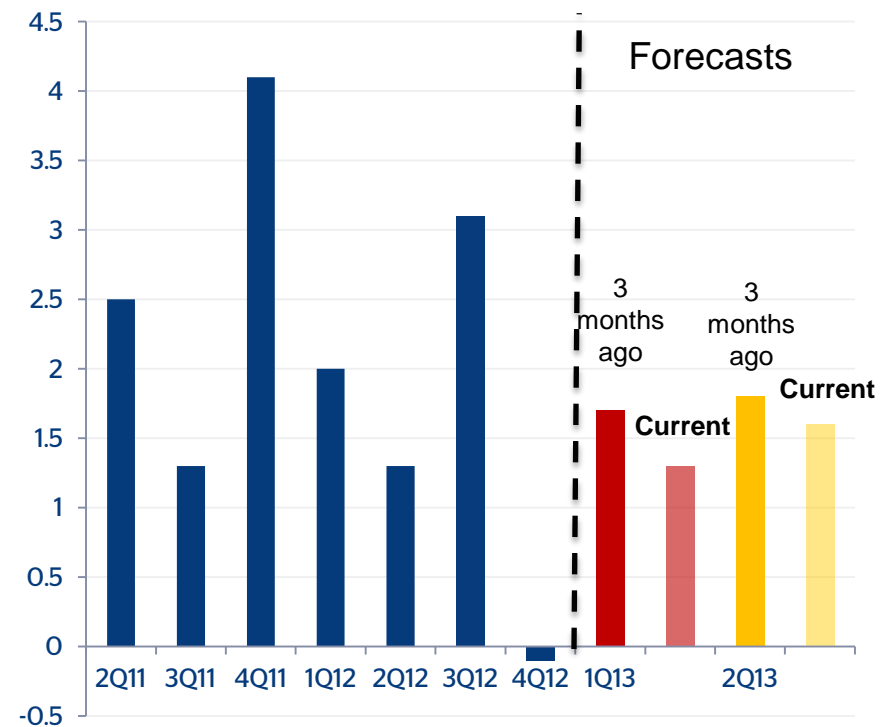
BBVA US Monthly Activity Index

4Q % Change



Real GDP Growth

QoQ SAAR, %

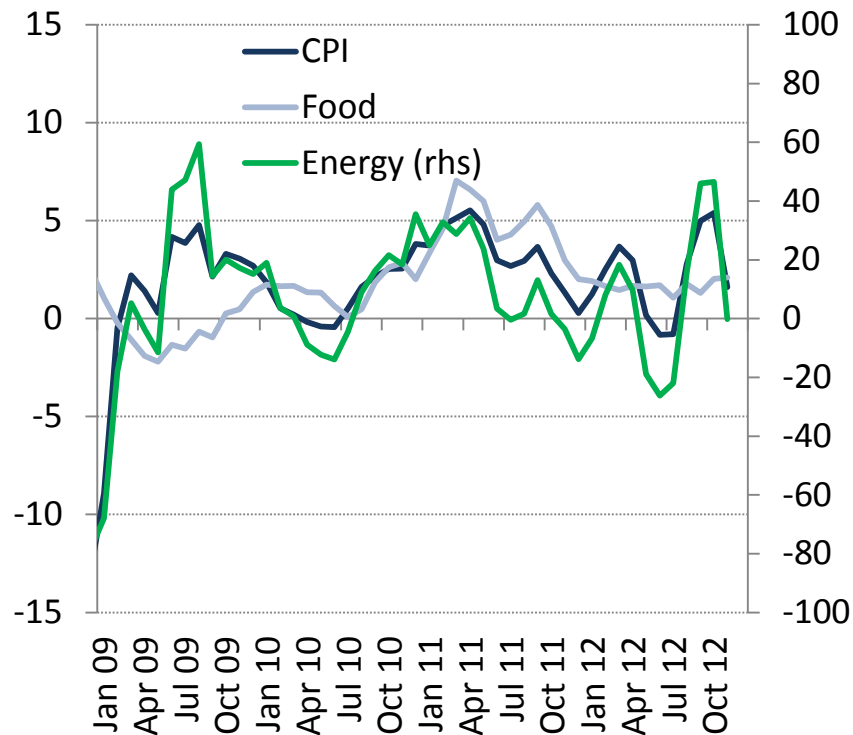


Inflation

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

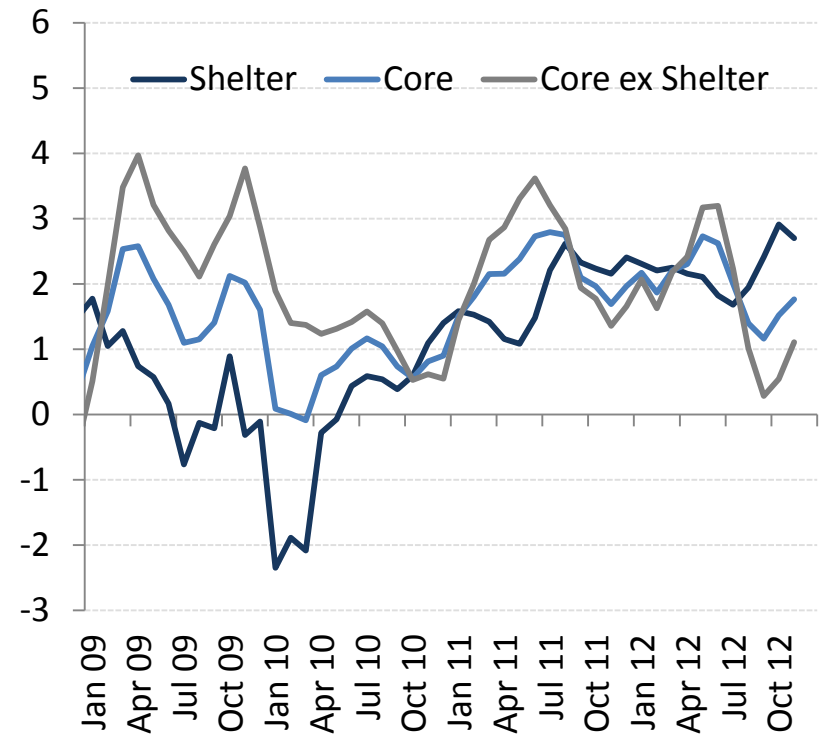
CPI Prices

3m % change, annualized



Core Prices

3m % change, annualized



Monetary Policy

Despite changes at the FOMC and disagreements, QE remains pretty much data dependent.

2012			2013			2014		
Board of Governors	Chairman	Ben S. Bernanke	Chairman	Ben S. Bernanke	Chairman	Ben S. Bernanke		
	Vice Chair	Janet L. Yellen	Vice Chair	Janet L. Yellen	Vice Chair	Janet L. Yellen		
	Governor	Elizabeth A. Duke	Governor	Elizabeth A. Duke	Governor	Elizabeth A. Duke		
	Governor	Daniel K. Tarullo	Governor	Daniel K. Tarullo	Governor	Daniel K. Tarullo		
	Governor	Sarah Bloom Raskin	Governor	Sarah Bloom Raskin	Governor	Sarah Bloom Raskin		
	Governor	Jeremy C. Stein	Governor	Jeremy C. Stein	Governor	Jeremy C. Stein		
	Governor	Jerome H. Powell	Governor	Jerome H. Powell	Governor	Jerome H. Powell		
Bank Presidents	New York	William C. Dudley	New York	William C. Dudley	New York	William C. Dudley		
	Richmond	Jeffrey M. Lacker	Chicago	Charles L. Evans	Cleveland	Sandra Pianalto		
	Atlanta	Dennis P. Lockhart	Boston	Eric S. Rosengren	Philadelphia	Charles I. Plosser		
	Cleveland	Sandra Pianalto	St. Louis	James Bullard	Dallas	Richard W. Fisher		
	San Francisco	John C. Williams	Kansas City	Esther L. George	Minneapolis	Narayana Kocherlakota		
Dovish 1		2	Center 3	4	Hawkish 5			

Baseline: No major changes

- Economic recovery picking up speed as the year progresses
 - Improved external conditions
 - Moderate fiscal impact in 1H13
 - Healthier financial market conditions
 - Slower deleveraging process
 - Ongoing recovery in the real estate sector
 - Potential for positive surprises
- Inflation within the Fed's target of 2%
 - Upward pressures from commodity and shelter prices
 - Elevated economic slack and stable inflation expectations
- Steepening of the yield curve and a more positive FOMC
 - Possible end of QE in 2013 and first rate hike in 4Q15
 - Portfolio rebalancing in favor of riskier assets

US Baseline Scenario

New vs. Previous*

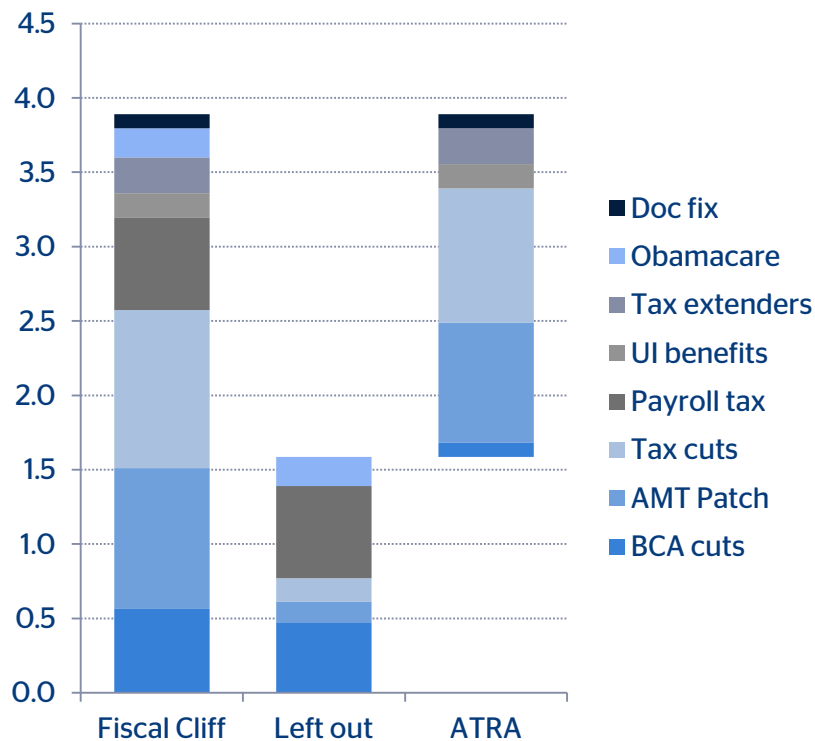
	2011	2012	2013	2014	2015	2016	2017
GDP new	1.8	2.2	1.8	2.3	2.5	2.7	2.6
old	1.8	2.1	1.8	2.3	2.5	2.7	--
CPI new	3.1	2.1	2.1	2.2	2.3	2.4	2.5
old	3.1	2.0	2.1	2.4	2.5	2.6	--
Core new	1.7	2.1	1.9	2.0	2.1	2.3	2.4
old	1.7	2.1	1.9	2.0	2.1	2.3	--
Fed new	0.25	0.25	0.25	0.25	0.50	1.50	2.50
[eop] old	0.25	0.25	0.25	0.25	0.50	1.5	2.5

Fiscal Situation

The fiscal deal avoids a large economic drag

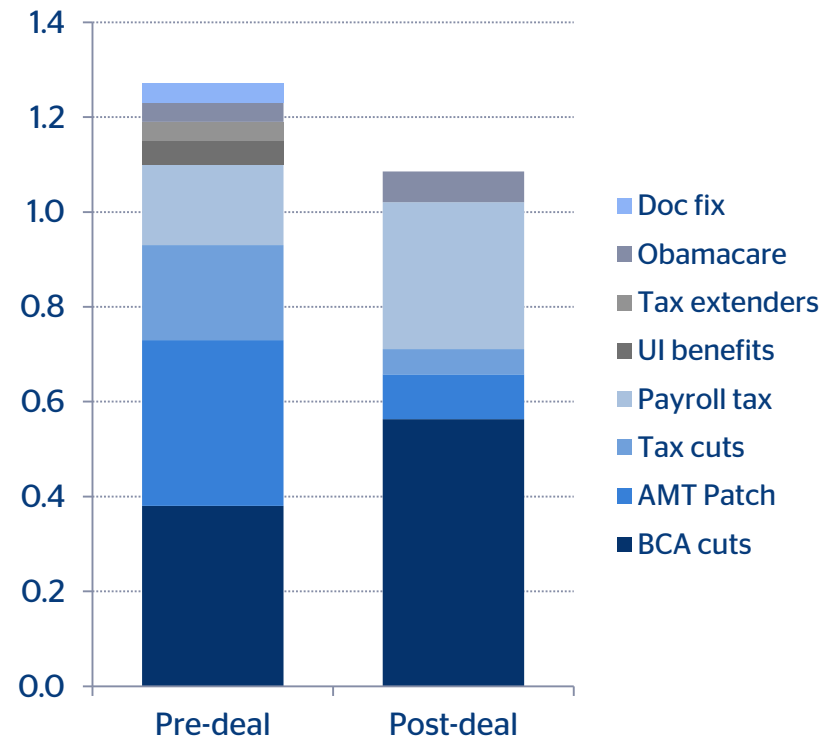
Size of the cliff

% of GDP, CY 2013



Economic Impact

% of GDP, CY 2013

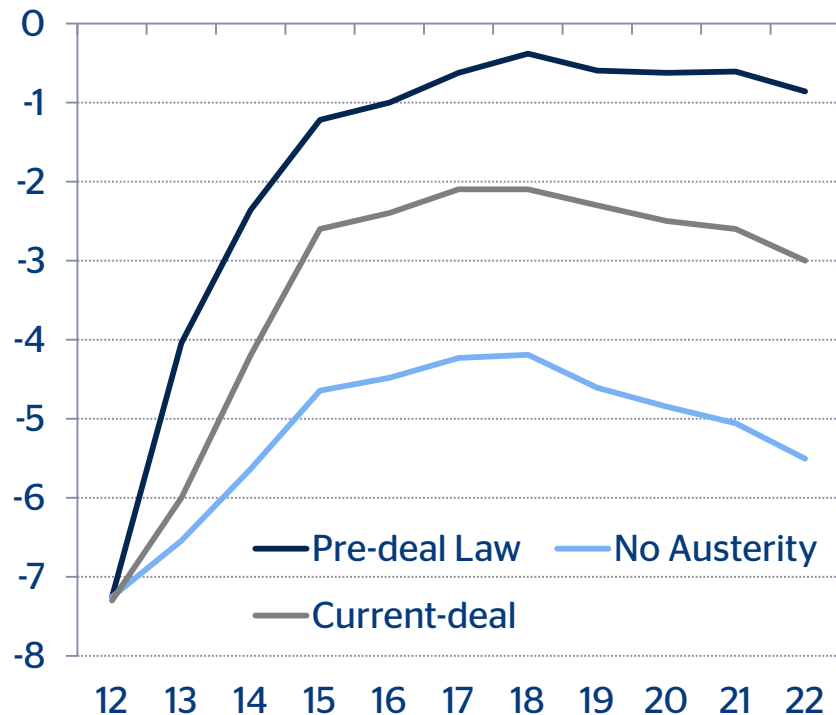


Fiscal Situation

And, in a relatively positive environment, provides debt stability

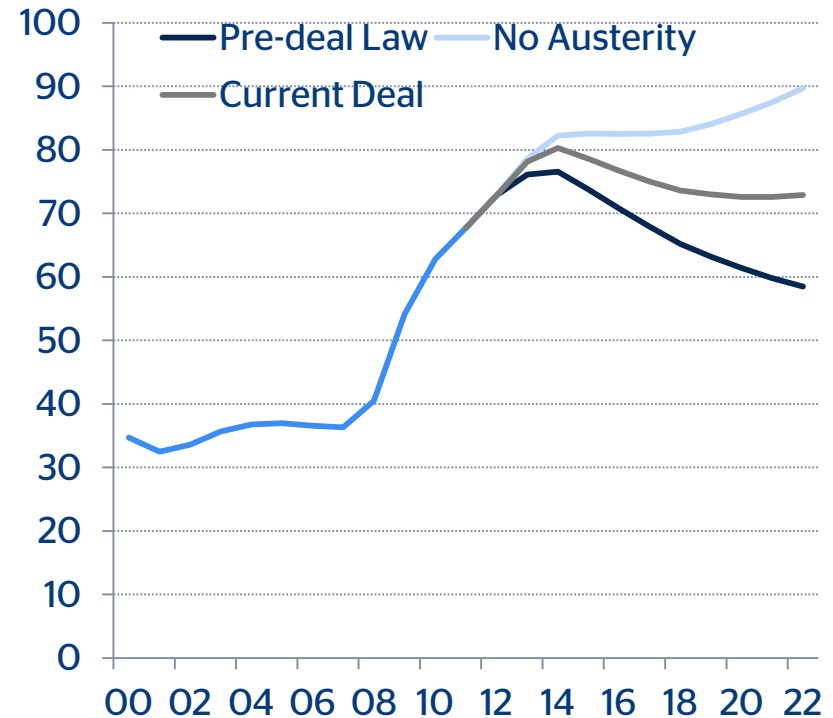
Budget Deficit

% of GDP



Debt held by the Public

% of GDP



Risk: Domestic concerns still relevant

- Economic recession

- Policy uncertainty shock
- Sudden reversal in financial and lending conditions
- Weaker business expectations and capital spending, along with declines in real income and employment
- Further deleveraging
- European crisis and slowdown in EMs
- Potential for long-term structural damage

- Deflationary pressures

- Downward pressures from commodity prices
- Significant economic slack and low inflation expectations

- Flat yield curve for a prolonged period under uncharted waters

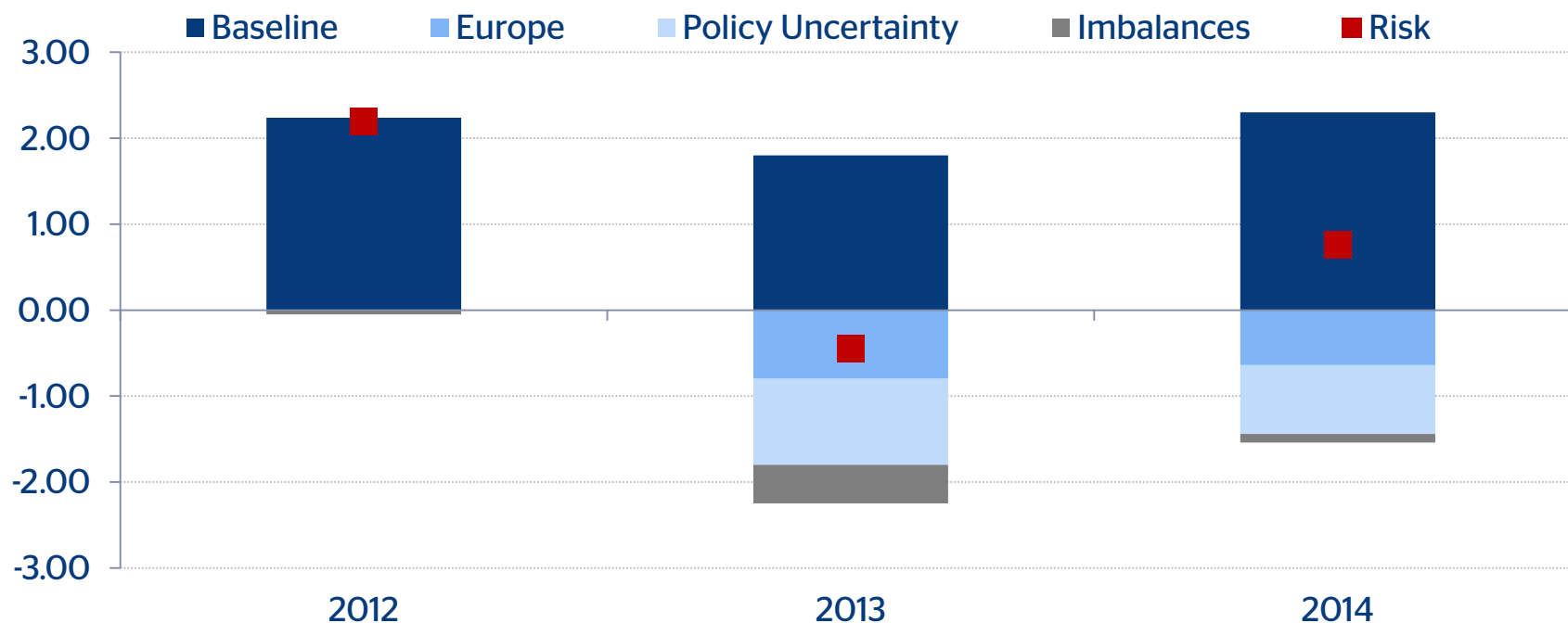
- Flight to safety
- Additional unconventional measures

- *Uncertainty on US credit rating quality (Potential sell off of US assets)*

GDP

The main risks to our outlook are the European crisis, policy uncertainty, and domestic imbalances

Real GDP (YoY % change)

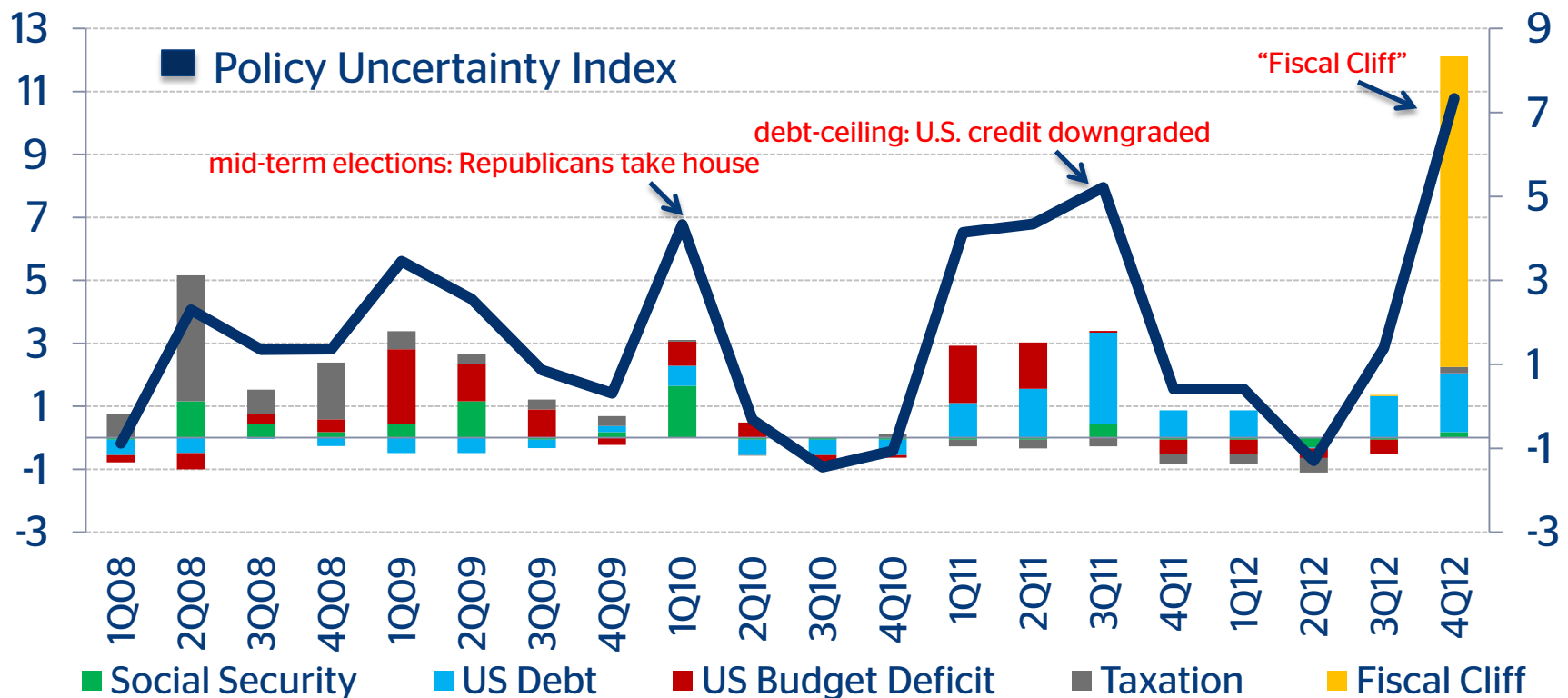


Policy Uncertainty

The prolonged “Fiscal Cliff” negotiations reignited US policy uncertainty.
Revisiting the debt-ceiling remains a key risk to recovery.

BBVA Policy Uncertainty Index & Decomposition

Decomposed uncertainty are normalized contribution to the Policy Index, Policy Uncertainty Index(right hand side): mean=0

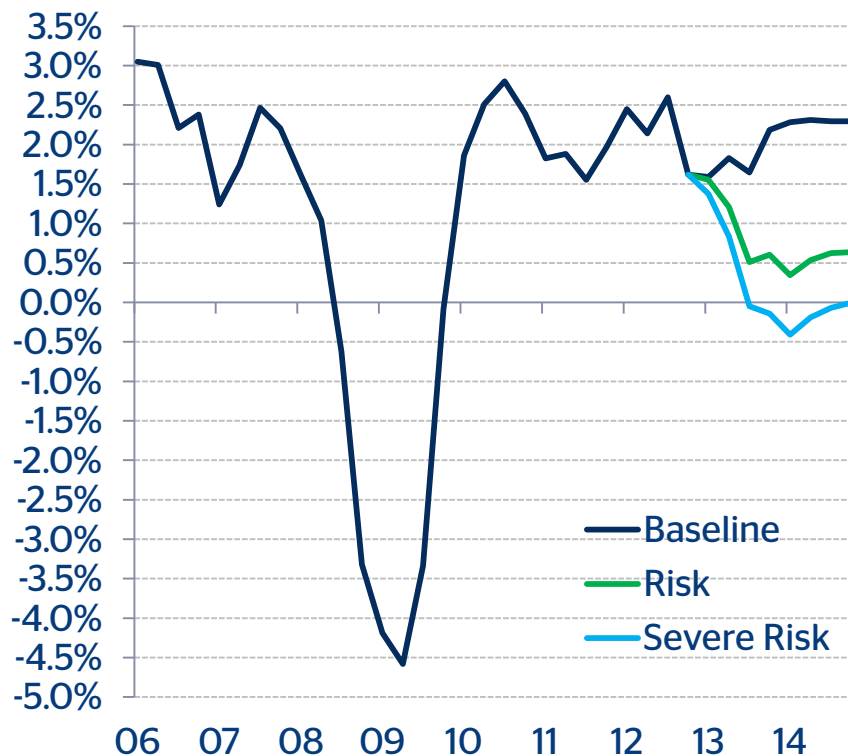


Direct Effects of Policy Uncertainty

Debt-Ceiling mismanagement could reduce GDP growth by 1.2% in 1H13

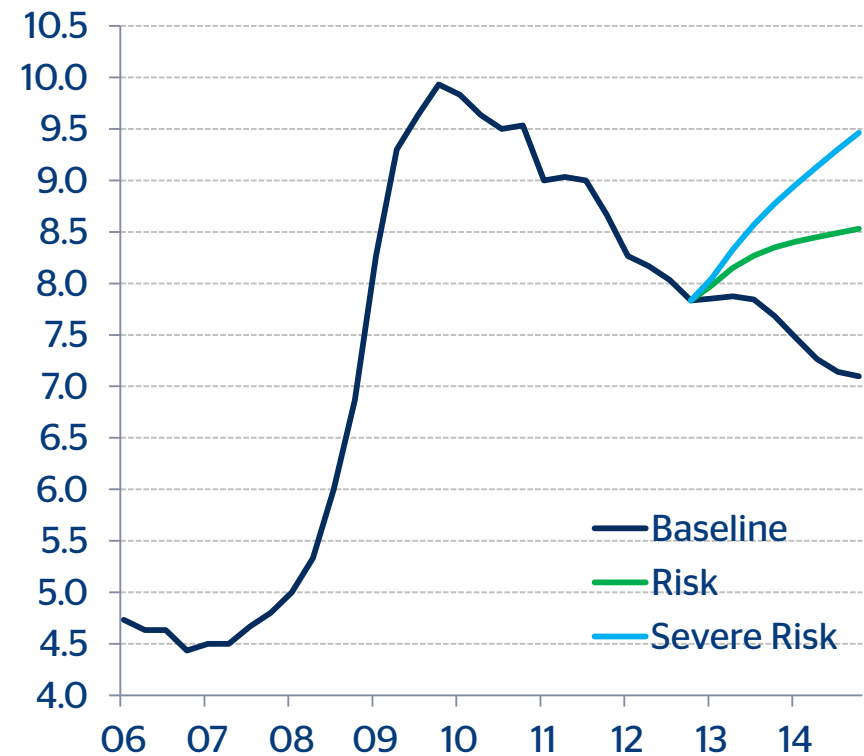
GDP Response to Policy Uncertainty

3 standard deviation shock assumed, year-over-year%



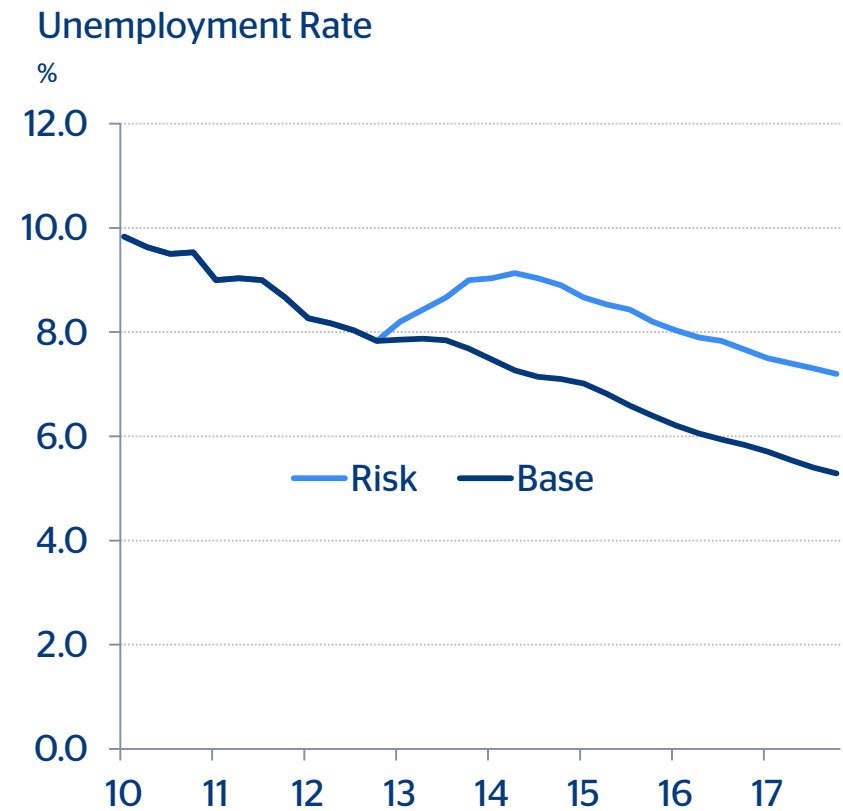
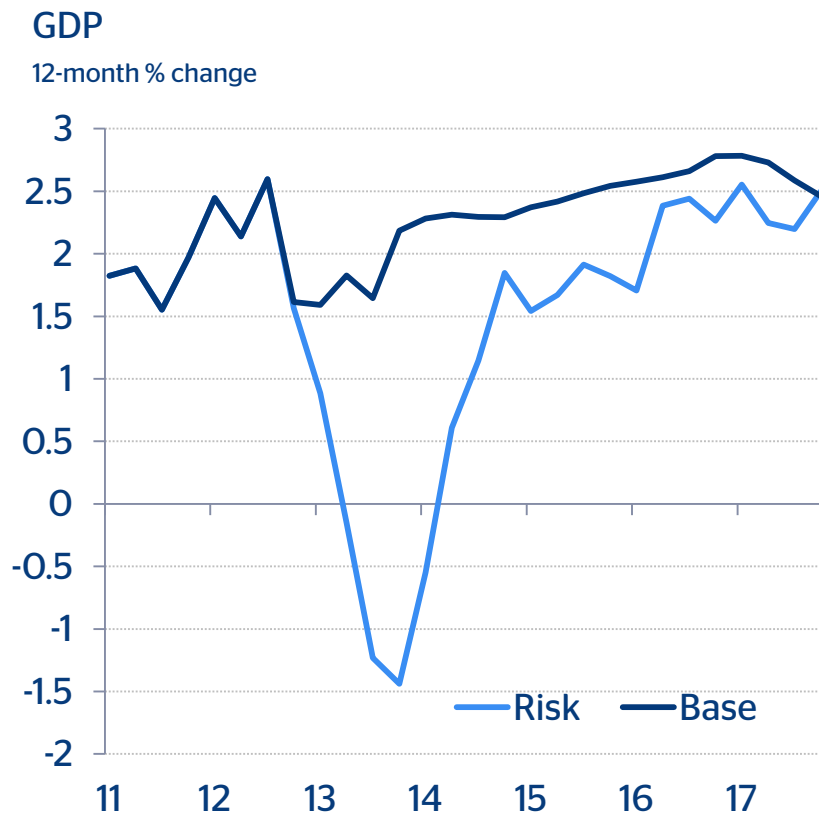
Unemployment Response to Policy Uncertainty

3 standard deviation shock assumed, %



GDP and Unemployment

The likelihood and potential magnitude of a double-dip recession has declined somewhat, yet looming uncertainty for 2013 is still a factor



US Risk Scenario

New vs. Previous*

	2011	2012	2013	2014	2015	2016	2017
GDP new	1.8	2.1	-0.5	0.8	1.7	2.2	2.4
old	1.8	2.0	-1.2	0.5	1.9	2.8	--
CPI new	3.1	2.1	-0.4	0.4	1.6	2.0	2.1
old	3.1	2.0	-0.6	0.8	1.9	2.2	--
Core new	1.7	2.1	1.1	1.2	1.6	1.9	2.0
old	1.7	2.1	1.1	1.2	1.8	2.3	--
Fed new	0.25	0.25	0.25	0.25	0.25	0.25	0.25
[eop] old	0.25	0.25	0.25	0.25	0.25	0.25	0.25

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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