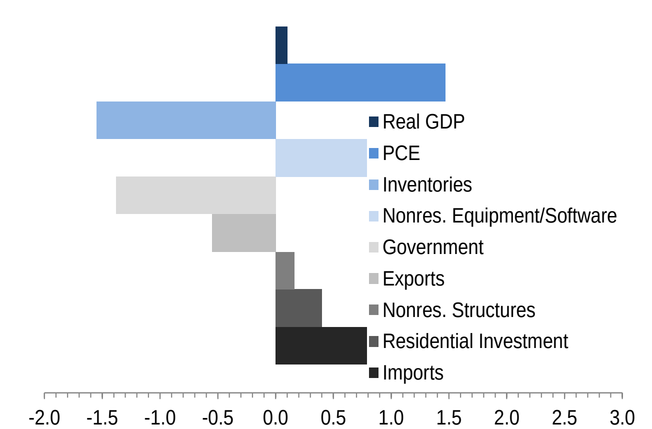
Economic Analysis
March 4, 2013

US Weekly Flash

Highlights

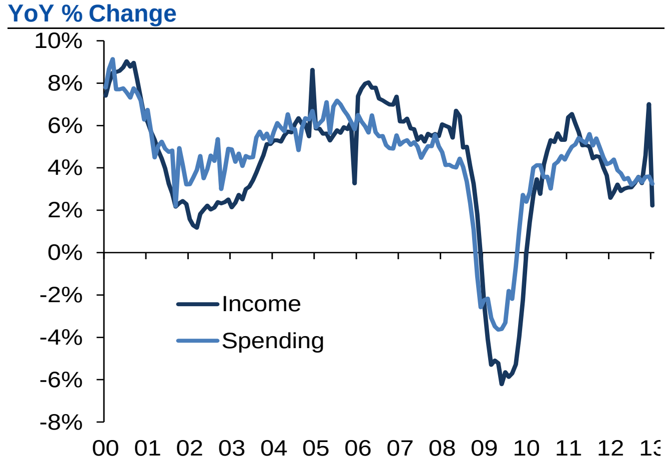
- **Government spending cuts are outdone by better trade on GDP revision**
  - After a slightly worrying negative GDP figure for the advanced 4Q12 estimate, preliminary figures show a reversal to a positive 0.1% on a QoQ seasonally-adjusted annualized basis. Government spending and private inventories had pushed down the advance figure and were revised down even further in the second report. Overall government expenditures declined 6.9% from the previous 6.6% drop in the first estimate as the initial spending cuts from fiscal negotiations were implemented. Private inventory investment was also revised down to -1.5%, though this could imply a rebuilding of inventories, and ultimately upward pressure on growth, for the first part of 2013. Personal consumption was also revised down slightly from 2.2% to 2.1%
  - While the above components weighed on the 4Q12 GDP figure, other components saw more positive revisions. Final sales of domestic product were revised up to 1.7% from the prior 1.1% for the quarter, still lower than the 3Q12 figure but matching the rate seen in 2Q12. Both nonresidential and residential fixed investment contributed a bit more to GDP growth in a positive manner. The second report was also bolstered by a better trade outcome for December. The trade deficit declined on account of stronger export growth, which subsequently boosted the contribution of net exports to GDP. Overall, this does not change our expectations for 2013 growth, with some momentum carrying over into 1H13 but then a pickup in activity later in the year once businesses and consumers adjust to new fiscal measures
- **Personal spending grows while income falls sharply after December's spike**
  - The personal income and spending report for January sheds light on exactly how consumers tried to avoid the worst of Washington's tax and spending fears. Consumption rose by 0.2% as individuals did not adjust their spending habits much in reaction to the expiring payroll tax cut that hit in January. The goods portion of consumption fell by 0.25% on lower durable goods consumption while the driver for spending came from the services sector, up 0.38%.
  - In general, the fact that consumption held up in January was somewhat of a surprise, particularly considering the report's counterpart. The 3.6% decline in personal income, the most in 20 years, was a mixture of actions that took place in December and a less sanguine beginning to 2013. The most abrasive cut to income was the reset to a 2% higher payroll tax that emerged from a final hour deal in Washington, raising the rate back to the pre-Bush level and cutting into disposable personal income immediately in January. Companies were fearful that other taxes and rates might be changed for the New Year so they doled out dividends to the tune of a 32% rise from November. Come January, that figure axiomatically had to decline and it did so by 34% as dividends returned to their regular schedules. The disposable income figure (income minus current taxes) shows the brunt of the damage: a decline of 3.9% due mostly to the payroll tax increase.

Graph 1
Contributions to Real GDP Growth
4Q12 Preliminary Estimate, SAAR Percentage Points



Source: US BEA & BBVA Research

Graph 2
Real Personal Income and Spending
YoY % Change



Source: US BEA & BBVA Research

Week Ahead

ISM Non-Manufacturing Index (February, Tuesday 8:30 ET)

Forecast: 55.1	Consensus: 55.0	Previous: 55.2

The ISM-Non-Manufacturing Index declined slightly to 55.2 in January despite better-than-expected hiring in the services sector. For February, we expect the index to remain strong but unflinching as the latest data show little movement in the underlying factors related to the report. Retail sales came in relatively flat in January with little indication that it will jump in February, a reflection of the business activity component of the ISM. Weekly retail sales indicators show mixed reports but the majority have the latter half of February showing growth. Coupled with the gains in the housing market, home goods and furnishings are likely to keep growing along with auto sales which have picked up within the last few months. The latest report on personal consumption suggested an increase in demand for services to start the year, which could give a boost to this index for the month.

International Trade Balance (January, Thursday 8:30 ET)

Forecast: $-41.0B	Consensus: $-43.0	Previous: $-38.5

Following the significant improvement in the U.S. trade deficit in December, a reversal is likely to take place in January as the latest data point to a slowdown in manufacturing and production export activity. A large driver in the December report was the export of fuels, specifically oil and natural gas. While U.S. production of oil and natural gas continues to rise, we expect that exports of fuels will emerge a bit weaker in January due to political headwinds and still sluggish growth abroad. However, the ISM manufacturing and services reports for January noted continued growth in export orders at a slightly faster pace than imports. Overall, we expect imports to remain relatively subdued due to the weaker dollar in January and ongoing demand for domestic goods such as vehicles and small equipment. With little pent up demand from the holiday season, a weaker import figure and ailing export demand will likely lead to a widening of the trade balance, albeit only for the short term, as trade begins to reignite global demand.

Nonfarm Payrolls & Unemployment Rate (February , Friday 8:30 ET)

Forecast: 152K, 7.9%	Consensus: 150K, 7.9%	Previous: 157K, 7.9%

Nonfarm payrolls are expected to rise in February at a similar pace as in January as economic indicators suggest little disruption in the workforce. February initial jobless claims show some increases in the number of those filing for unemployment benefits, though the monthly average thus far is pretty much on par with January. Consumer confidence reports suggest little change in individuals' outlook on job availability, though overall sentiments have improved since December. The Dallas, New York, Richmond and Philadelphia branches of the Federal Reserve have reported improving employment conditions for February at varying degrees in the manufacturing sector. While the 6-month outlook remains relatively strong, February continues to show little substantive evidence for a decline in the unemployment rate below the 7.8% reached late in 2012. The Federal Reserve has hinted that 2013 is poised to be a strong year for employment but most Fed representatives believe that growth will accelerate later in the year as budgetary issues subside.

Wholesale Inventories (January, Friday 10:00 ET)

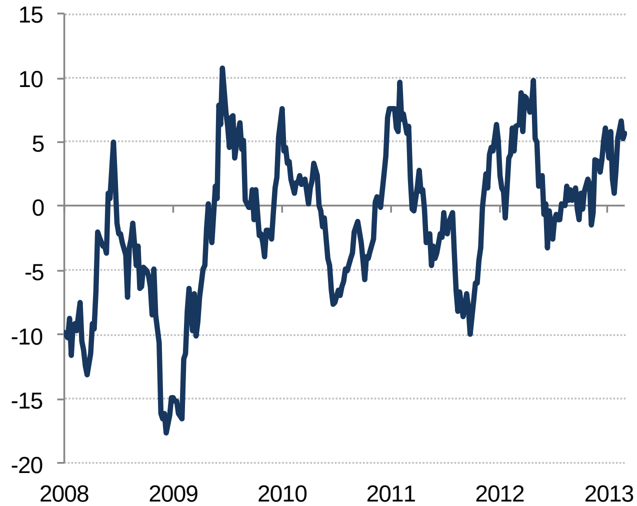
Forecast: 0.3%	Consensus: 0.3%	Previous: -0.1%

Wholesale inventories are likely to remain in decline as manufacturing reports show subdued gains for January, but still an improvement over December's decline. Regional Federal Reserve manufacturing surveys across the districts show reduced inventories as shipments rose with little restocking from new orders. For example, the Philly Fed survey noted a drop of 6.5 points on its inventory index for January with a concurrent decline of 4.3 for new orders. This simultaneous emptying of inventories was survey wide, save a few smaller areas, and will likely cause the wholesale inventories report to show some signs of only modest growth until demand picks up again and warehouses are refilled. The durable goods report for January showed that, excluding transportation, its measure of inventories also decline by 0.1% which continues its month-to-month decline since November. However, we do expect that demand for durable and nondurable goods will increase over the coming months as new orders on both Fed surveys and the durable goods report have risen.

Market Impact:

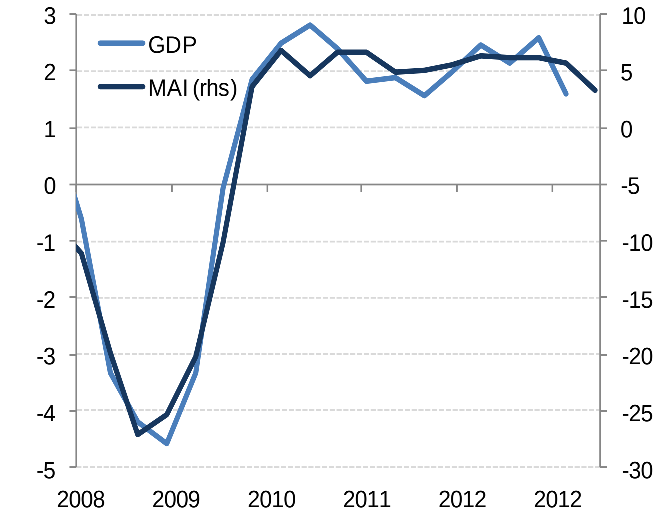
This week continues the trend of large economic variables that play a major role in assessing the strength of the current economic recovery. The U.S. trade deficit will be released midweek and is expected to show a slight increase due to changing global demand. Then comes employment for February which is expected to come back mildly changed as there is little evidence to suggest major moves throughout the economy in terms of employment. While these two factors always warrant some market reaction, the week will be shadowed by the sequester engagement in Washington and a continued ear to Congress or the senate for attempts to reduce the cuts.

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



Source: BBVA Research

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

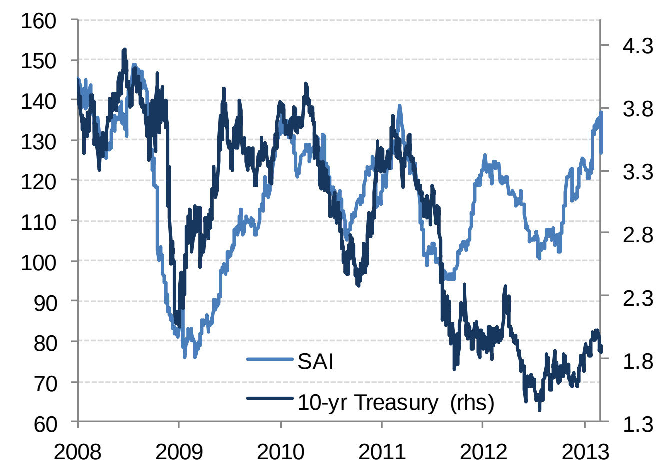


Source: BBVA Research & BEA

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

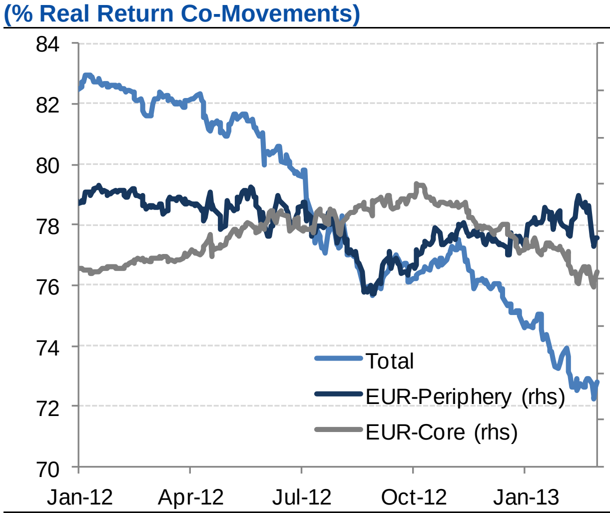
Source: BBVA Research

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



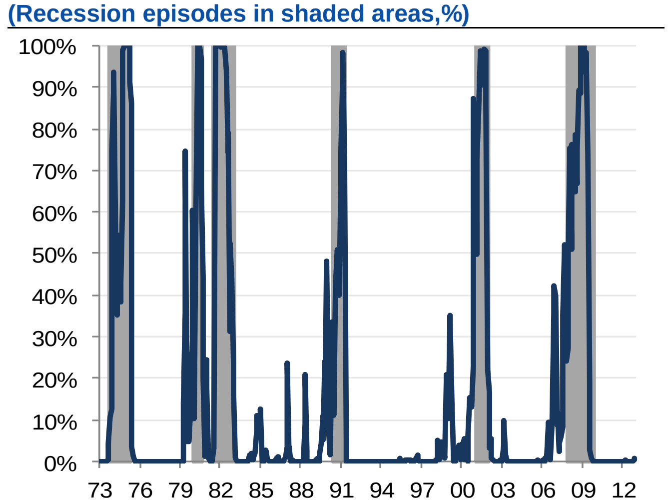
Source: Bloomberg & BBVA Research

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



Source: BBVA Research

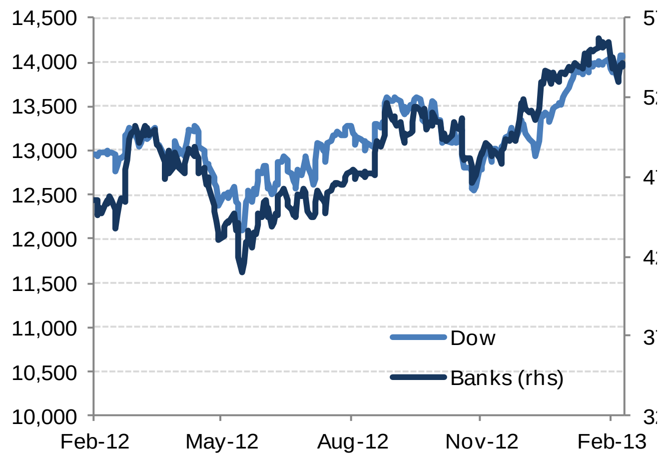
Graph 8
BBVA US Recession Probability Model
(Recession episodes in shaded areas,%)



Source: BBVA Research

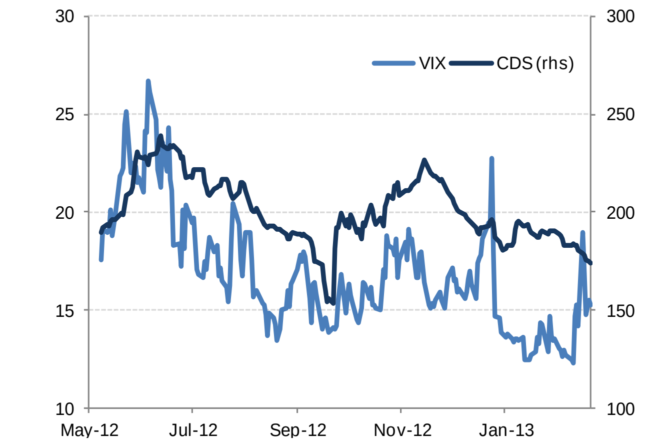
Financial Markets

Graph 9
Stocks
(Index, KBW)



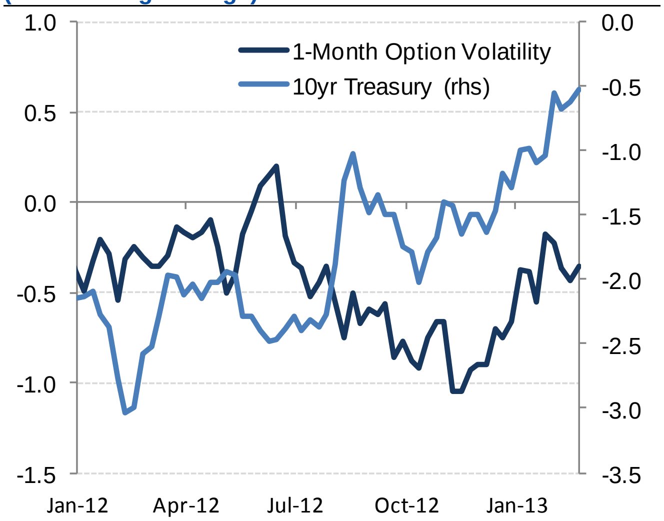
Source: Bloomberg & BBVA Research

Graph 10
Volatility & High-Volatility CDS
(Indices)



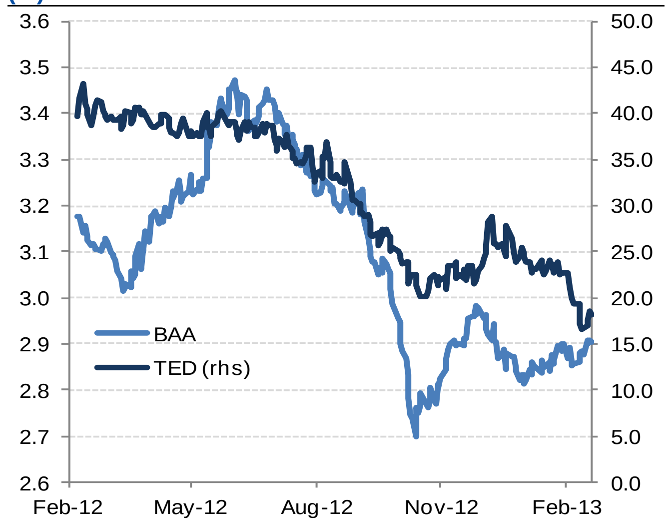
Source: Bloomberg & BBVA Research

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



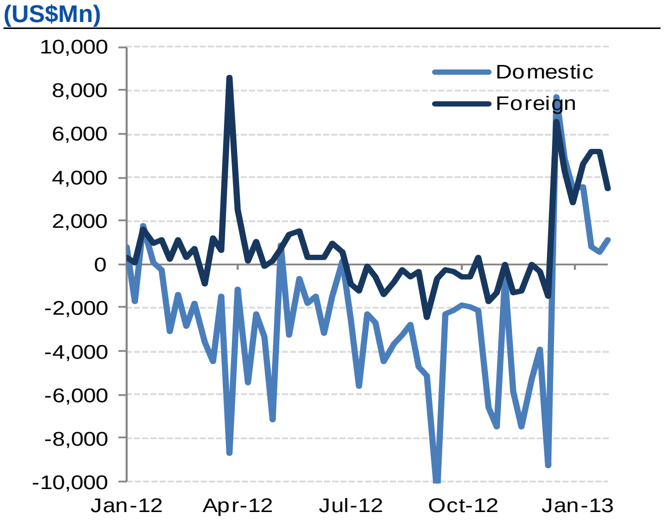
Source: Haver Analytics & BBVA Research

Graph 12
TED & BAA Spreads
(%)



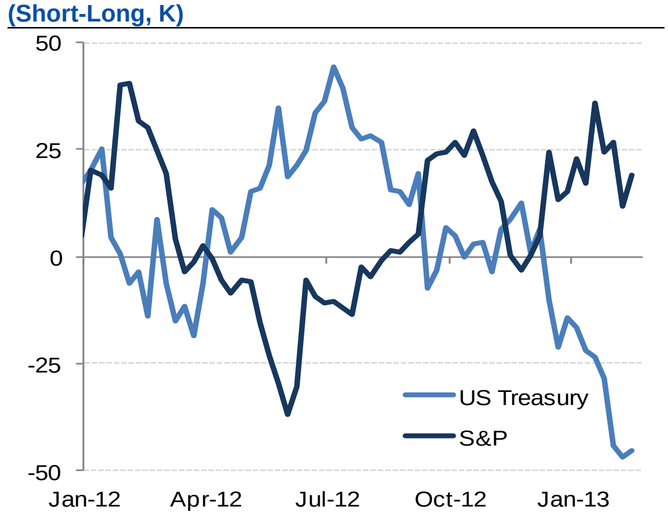
Source: Bloomberg & BBVA Research

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



Source: Haver Analytics & BBVA Research

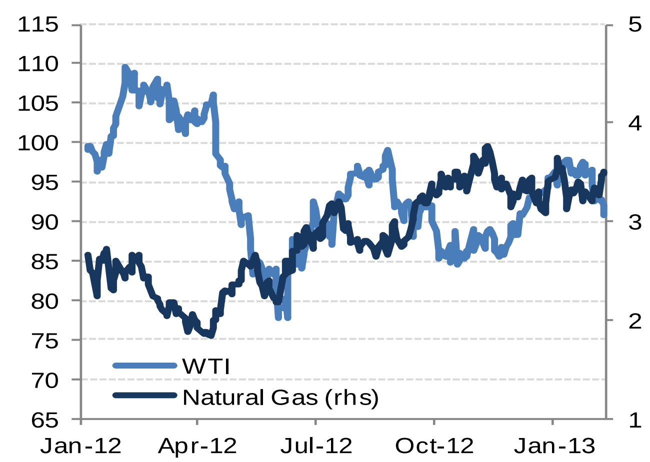
Graph 14
Total Reportable Short & Long Positions
(Short-Long, K)



Source: Haver Analytics & BBVA Research

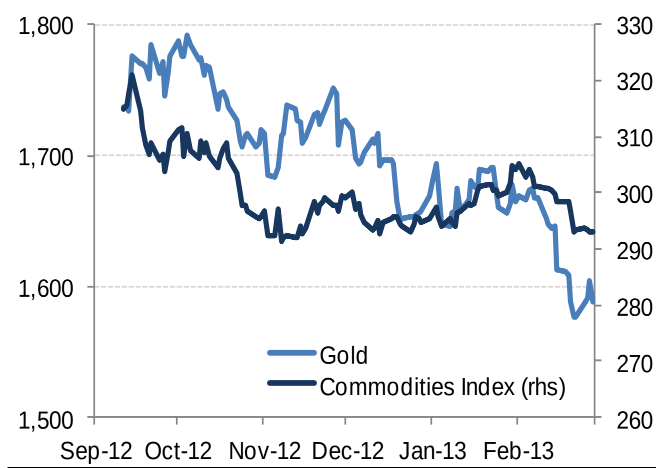
Financial Markets

Graph 15
Commodities (Dpb & DpMMBtu)



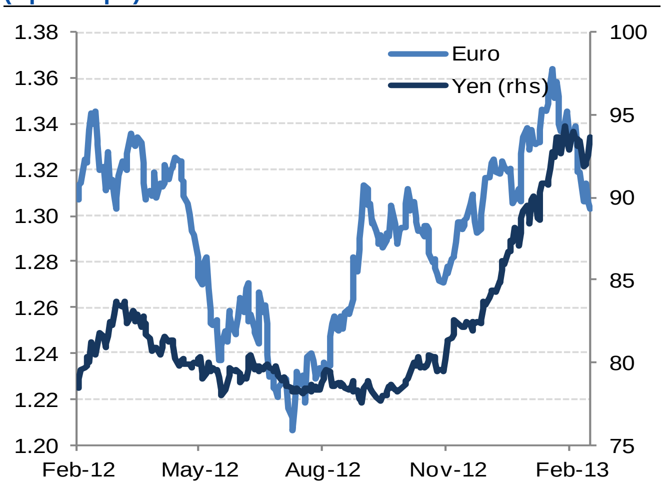
Source: Bloomberg & BBVA Research

Graph 16
Gold & Commodities (US$ & Index)



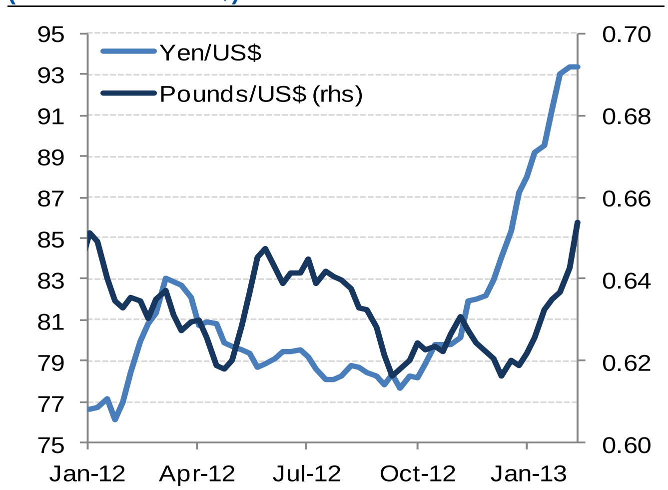
Source: Haver Analytics & BBVA Research

Graph 17
Currencies (Dpe & Ypd)



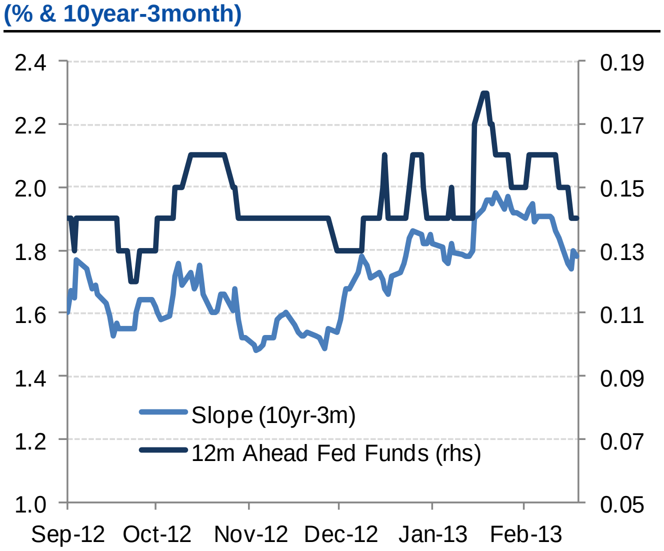
Source: Bloomberg & BBVA Research

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



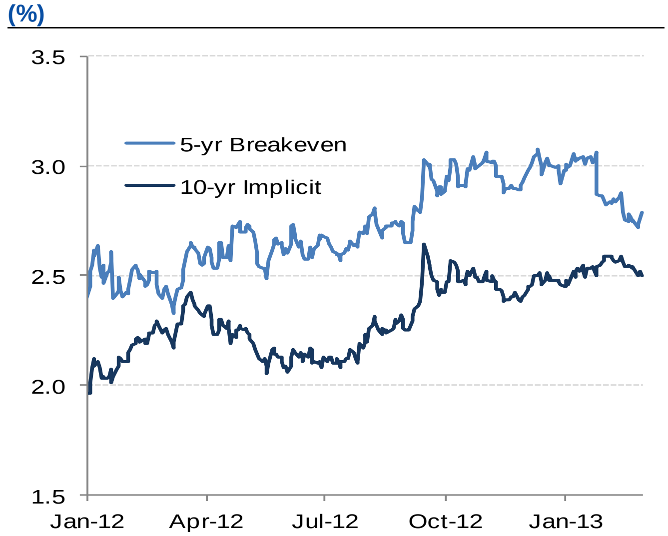
Source: Haver Analytics & BBVA Research

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)	14.50	14.50	14.46	14.10
New Auto (36-months)	2.48	2.44	2.47	3.54
Heloc Loan 30K	5.28	5.38	5.38	5.54
5/1 ARM *	2.61	2.64	2.70	2.83
15-year Fixed Mortgage *	2.76	2.77	2.81	3.17
30-year Fixed Mortgage *	3.51	3.56	3.53	3.90
Money Market	0.48	0.48	0.50	0.50
2-year CD	0.74	0.74	0.77	0.75

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

Table 1
Key Interest Rates (%)

	Last	Week ago	4-Weeks ago	Year ago
1M Fed	0.14	0.16	0.14	0.11
3M Libor	0.28	0.29	0.45	0.48
6M Libor	0.46	0.46	0.65	0.75
12M Libor	0.75	0.76	0.98	1.06
2yr Sw ap	0.38	0.40	0.42	0.52
5yr Sw ap	0.91	0.98	1.04	1.10
10Yr Sw ap	1.95	2.04	2.10	2.06
30yr Sw ap	2.93	3.01	3.05	2.80
30day CP	0.17	0.16	0.16	0.37
60day CP	0.19	0.18	0.18	0.44
90day CP	0.17	0.16	0.20	0.48

Source: Bloomberg & BBVA Research

Quote of the Week

Chairman of the Federal Reserve Ben Bernanke
Testimony to the FOMC
February 26, 2013

"*We do not see the potential costs of the increased risk-taking in some financial markets as outweighing the benefits of promoting a strong economic recovery. Inflation is currently subdued, and inflation expectations appear well anchored.*"

Economic Calendar

Date	Event	Period	Forecast	Survey	Previous
5-Mar	ISM New York	FEB	55.3	-	56.7
5-Mar	ISM Non Manufacturing Index	FEB	55.1	55.0	55.2
6-Mar	ADP Employment Report	FEB	167K	170K	192K
6-Mar	Factory Orders	JAN	-1.0%	-2.2%	1.8%
7-Mar	International Trade	JAN	$-41.0B	$-43.0B	$-38.5B
7-Mar	Initial Jobless Claims	3-Mar	332K	355K	344K
7-Mar	Continued Claims	24-Feb	3060K	3115K	3074K
8-Mar	Unemployment Rate	FEB	7.9%	7.9%	7.9%
8-Mar	Change in Nonfarm Payrolls	FEB	152K	160K	157K
8-Mar	Change in Private Payrolls	FEB	161K	167K	166K
8-Mar	Avg Hourly Earnings	FEB	0.2%	0.2%	0.2%
8-Mar	Wholesale Trade	JAN	0.3%	0.3%	-0.1%

Forecasts

	2011	2012	2013	2014	2015
Real GDP (% SAAR)	**1.8**	**2.2**	1.8	2.3	2.5
CPI (YoY %)	**3.1**	**2.1**	2.1	2.2	2.3
CPI Core (YoY %)	**1.7**	**2.1**	1.9	2.0	2.1
Unemployment Rate (%)	**8.9**	**8.1**	7.8	7.2	6.7
Fed Target Rate (eop, %)	**0.25**	**0.25**	0.25	0.25	0.50
10Yr Treasury (eop, % Yield)	**1.98**	**1.72**	2.35	2.80	3.37
US Dollar/ Euro (eop)	**1.32**	**1.31**	1.32	1.32	1.36

Note: Bold numbers reflect actual data

Kim Fraser
Kim.Fraser@bbvacompass.com

Alejandro Vargas
Alejandro.Vargas@bbvacompass.com

BBVA RESEARCH | 2001 Kirby Drive, Suite 31, Houston, Texas 7701 | Tel.: +1 713 831 7345 | www.bbvaresearch.com