

US Weekly Flash

Highlights

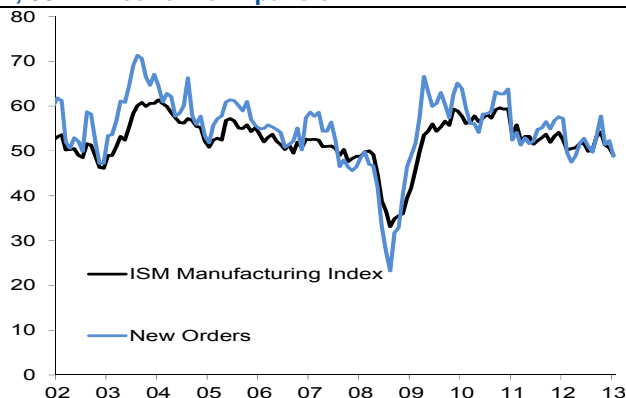
- ### Manufacturing Activity Contracts on Weak New Orders and Output in May

- Falling below 50 in May for the first time since last November, the ISM manufacturing index posted its lowest monthly figure since June 2009 and a look at the underlying factors doesn't bode well for upcoming releases. The breakdown of the index showed a weak state for manufacturing activity in May as the new orders component, which in April increased to 52.3, fell to 48.8 – the lowest level since last July. With inventories climbing to 49.0 in April from 46.5, the situation looks difficult as increased inventory could lead to reduced production in the future as firms try to get rid of existing stockpile.
 - The prequel to new orders, current production, also fell dramatically. The component fell below 50 to 48.6 which is its lowest reading in four years as output continues to falter on weaker domestic and global demand. However, there was some solace from the employment index which declined only slightly from 50.2 to 50.1 in May, relatively minimal compared to the rest of the components. While one month of data is seldom indicative of a trend, we do not expect the ISM index to return to growth immediately but remain close to the 50 threshold.

- ### Unemployment Rate Rises as Labor Market Grows in May

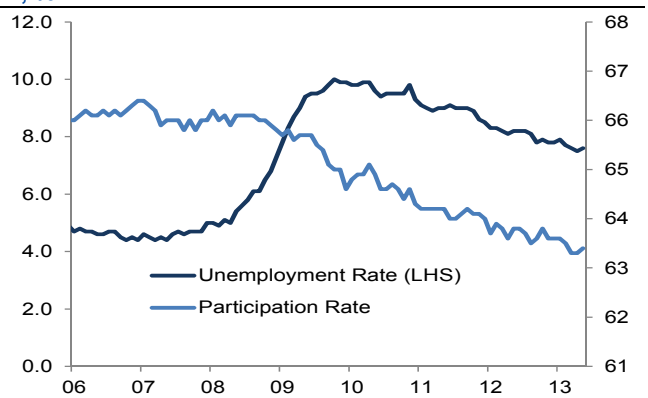
- The employment report for May exceeded expectations in many ways, with payrolls stronger than expected and more people entering back into the labor force. Nonfarm payrolls increased 175K following a downward revision to April's figures, from 165K to 149K. Nevertheless, with private payrolls in May up 178K, there can be no doubt that this jobs report was better than expected. Within the goods producing component, the notion that 2Q13 would bring slower momentum in terms of growth persists. The manufacturing sector which fell for the third consecutive month, down 8K in May as ISM and durable goods reports continue to point toward a deceleration in the sector. On the positive side, construction shrugged off its decline from the month before and added 7K to its ranks as the housing market continues to demand labor. Financial activities managed a slight increase while professional and business services continued to dominate the rise in job demand, adding 57K. Despite the stronger than expected payroll growth, the unemployment rate jumped back up to 7.6%. The participation rate nudged up a tenth of a percent to 63.4% and the labor force gained 420K new workers. This edges the labor force back to its all-time high after concerns that people were leaving at a discouraging rate as those closer to the retirement age were choosing to leave early.
 - Overall, May's report was mixed in terms of how we view the employment situation in 2Q13. Although payrolls rose more than anticipated, the revision to April brings the quarter's average almost back to its prior level of closer to the 162K level. Nevertheless, given the strong increase in service sector employment and the rise in the labor force, there are signs that the situation is improving.

Graph 1
ISM Manufacturing Index & New Orders
SA, 50+ = Economic Expansion



Source: Institute for Supply Management & BBVA Research

Graph 2
Unemployment and Participation Rates
SA, %



Source: BLS & BBVA Research

Week Ahead

Initial Jobless Claims (June 8th, Thursday 8:30 ET)

Forecast: 335K

Consensus: 345K

Previous: 346K

Initial jobless claims for the week ending on June 8th are expected to move only slightly as the ebb and flow of claims continues. While the overall figure determined for the claims is hard to predict, the 4-month moving average tends to be more indicative of which direction the trend has been moving. As of late the trend line has extended upward as a large spike late in May pushed the running average up and the movement downward has yet to happen. With that in mind, there is some room for a decrease in the claims number as the labor market continues to add jobs at a moderate clip. While the jobless claims figures are difficult to predict on a weekly basis, the continued claims aspect of the report has been on a more visible trend downward. Dropping to 2.976M last week, the figure has fallen consistently for months with only a few unexpected reversals. However, this is not necessarily indicative of more people becoming employed – it could just signal an end to benefits for long-term unemployed individuals.

Retail Sales, Ex. Autos (May, Tuesday 10:00 ET)

Forecast: 0.6%, 0.4%

Consensus: 0.4%, 0.3%

Previous: 0.1%, -0.1%

Retail sales are expected to accelerate in May as consumers remain confident about the coming months and seasonal shifts prompt a rise in spending. During the weaker months that followed the payroll tax increase, consumer activity was muted somewhat as they grappled with a hit to disposable income. However, consumption has remained markedly resilient and we expect this to show in the retail sales figure for May. The ICSC Goldman Sachs retail sales weekly index showed some signs of growth throughout the past few weeks and its YoY rate rose in comparison to prior months. A gradual decline in consumer hesitation with regard to economic woes will help to drive sales throughout the month. As the summer approaches and economic conditions improve, consumer activity will improve and the pent up demand from the prior quarter should prove to induce better sales in the coming months. Coupled with record high equity markets and a favorable currency, it is likely that retail sales will begin to show signs of improvement.

Industrial Production & Capacity Utilization (May, Friday 8:30 ET)

Forecast: -0.2%, 77.7%

Consensus: 0.2%, 77.9%

Previous: -0.5%, 77.8%

Despite the optimism that some of the Federal Reserve surveys had conveyed about the outlook for manufacturing, May will likely emerge weak with regard to industrial production. Following the downward trend in the sector's activity, industrial production may decline for the second straight month as leading indicators for the report are not showing much movement over last month. The Federal Reserve surveys tend to leading indicators and suggest that the overall picture for manufacturing has continued to decline, with the ISM adjusted figures in contracting territory. The Philadelphia Fed survey dropped again as a less optimistic outlook pulled down the production and employment indices. General conditions in May for the Empire State manufacturing survey also fell declined as a similar situation pulled down current manufacturing activity for the area. The recently released ISM manufacturing index for May dropped below 50 to its lowest reading in four years, with shipments and production declining at a significant clip. Given the weaker outlook from both the Federal Reserve surveys and the ISM release, we expect both industrial production and capacity utilization to decline in May.

Consumer Sentiment (June, Friday 8:30 ET)

Forecast: 85.2

Consensus: 84.5

Previous: 84.5

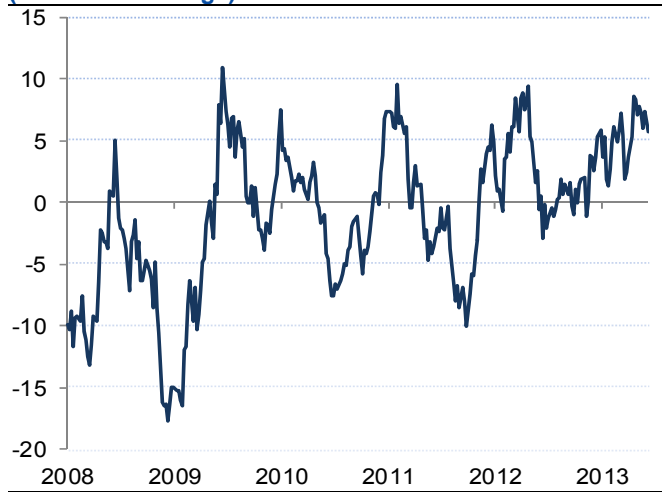
The University of Michigan's consumer sentiment survey is expected to increase given the recent data that has emerged coupled with the growing optimism behind future growth. Although, as of late, the manufacturing sector has shown signs of marked weakness, the service industry, which makes up 68% of GDP, has shown relative resilience in the face of government expenditure reduction and manufacturing weakness. Retail sales are, despite the payroll tax increase, still on the rise and consumer credit continues to show signs of consumer activity. While these levels are still far from their peaks, they do give a pulse in terms of the consumers' confidence in the economy and of their own finances. With that in mind, we expect that consumer confidence should be on the rise for the first report in June.

Market Impact

This week will highlight an interesting mixture of private sector growth in terms of manufacturing and services. After the ISM declined below 50 to indicate contraction, the manufacturing industry seems poised to relay even more negative news in the form of weaker industrial production data. However, to bolster the services industry, we are expecting an upward push for retail sales as the summer season finally takes grip across the U.S. and consumers emerge from their winter cocoons. To evidence that, consumer sentiment is expected to rise and should continue to shift upward in a stable manner as the economy recovers, keeping markets relatively stable as they await further announcements from the Fed later on in the month.

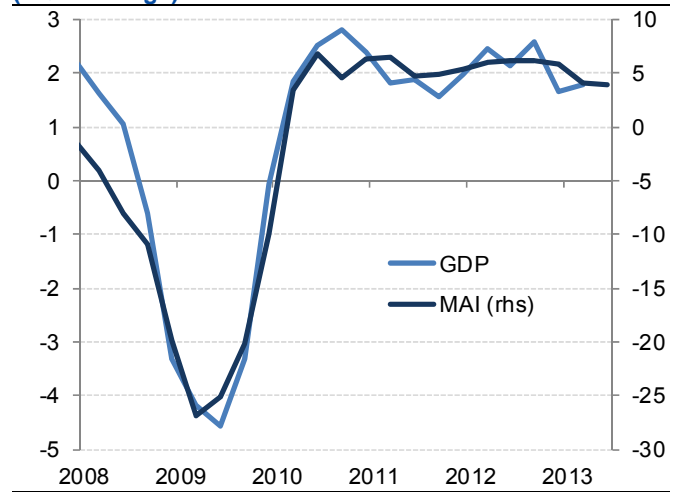
Economic Trends

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



Source: BBVA Research

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



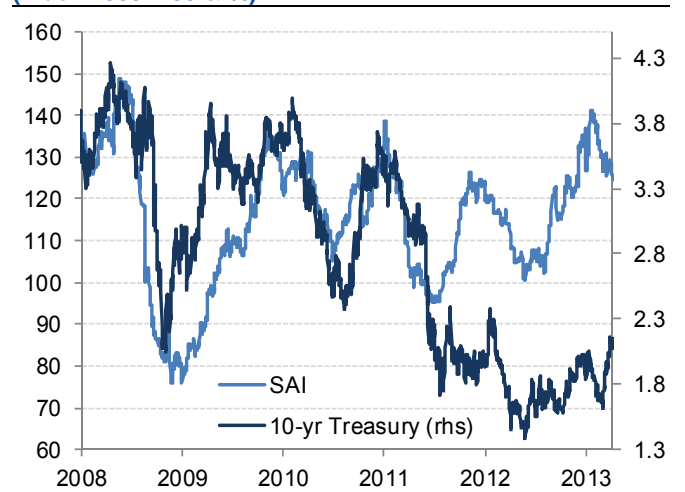
Source: BBVA Research & BEA

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



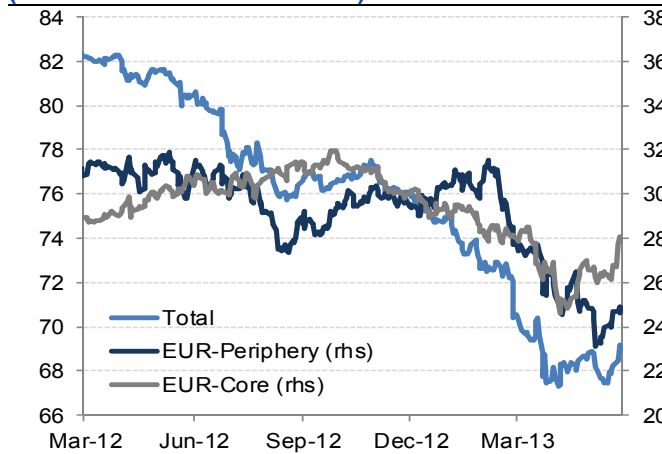
Source: BBVA Research

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



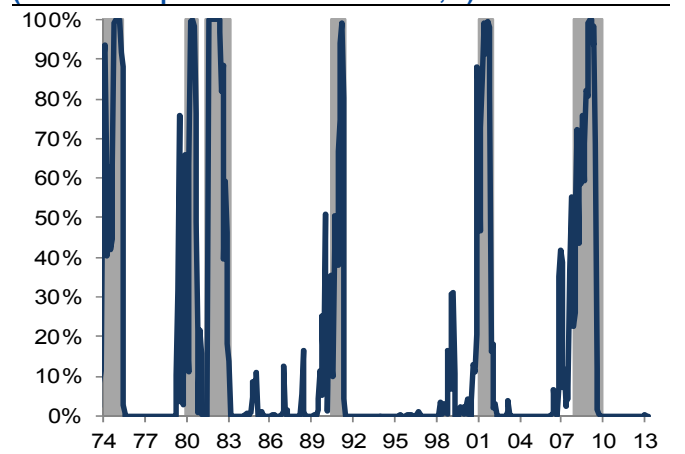
Source: Bloomberg & BBVA Research

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



Source: BBVA Research

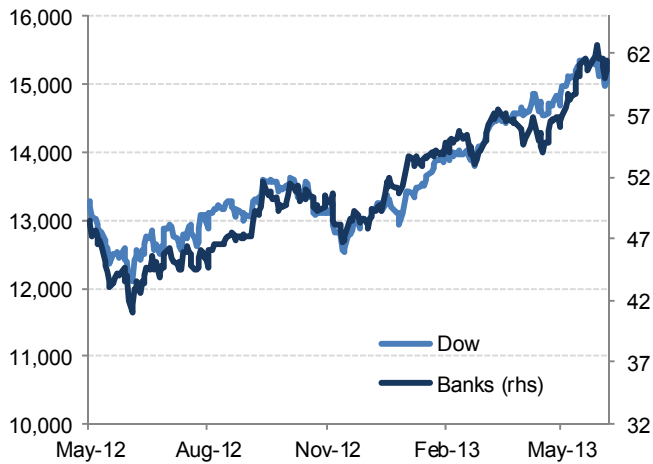
Graph 8
BBVA US Recession Probability Model
 (Recession episodes in shaded areas, %)



Source: BBVA Research

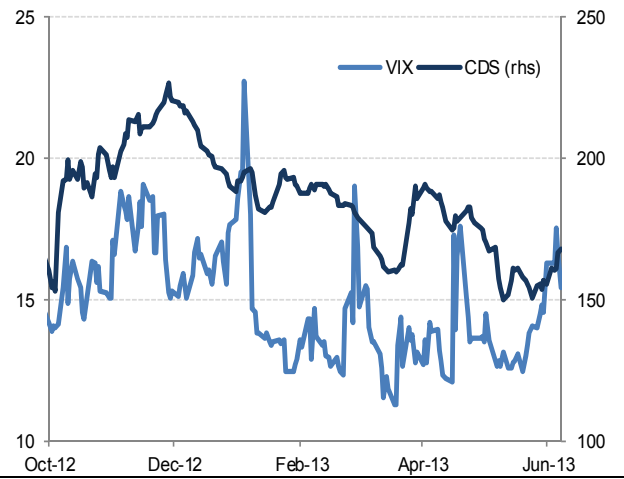
Financial Markets

Graph 9
Stocks
(Index, KBW)



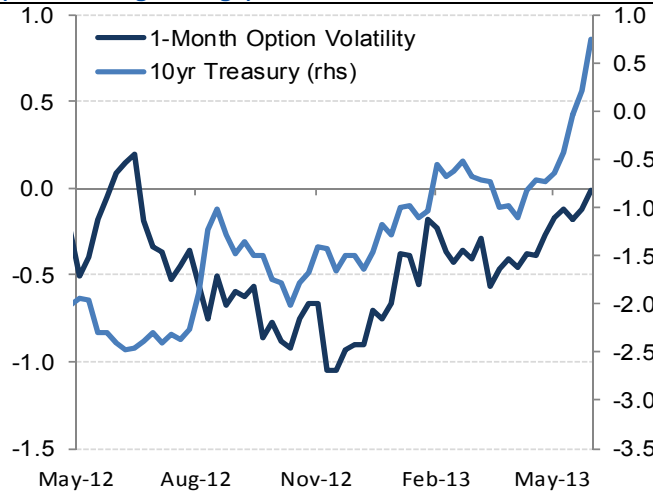
Source: Bloomberg & BBVA Research

Graph 10
Volatility & High-Volatility CDS
(Indices)



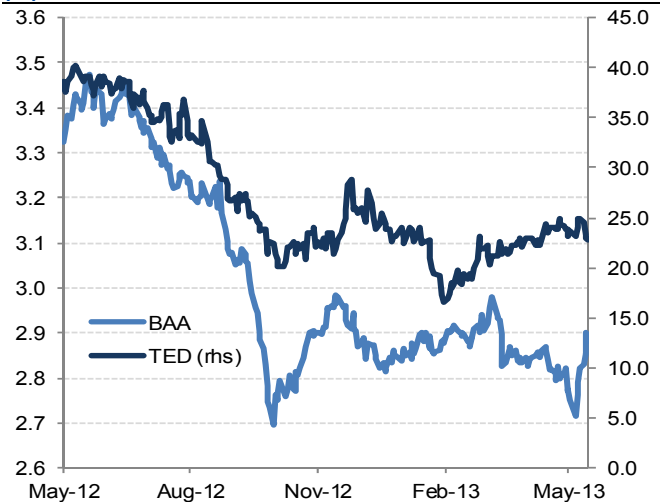
Source: Bloomberg & BBVA Research

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



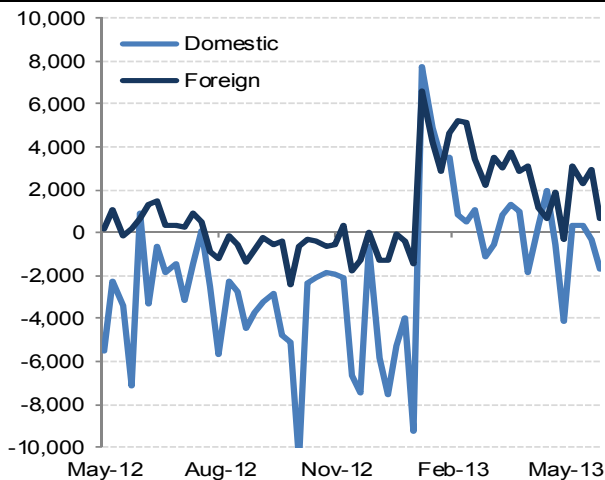
Source: Haver Analytics & BBVA Research

Graph 12
TED & BAA Spreads
(%)



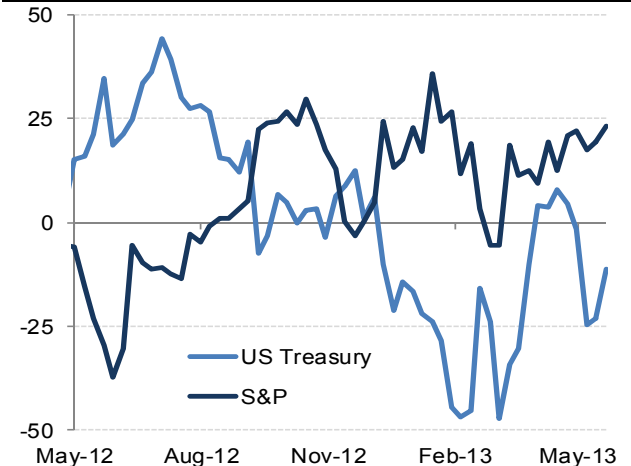
Source: Bloomberg & BBVA Research

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



Source: Haver Analytics & BBVA Research

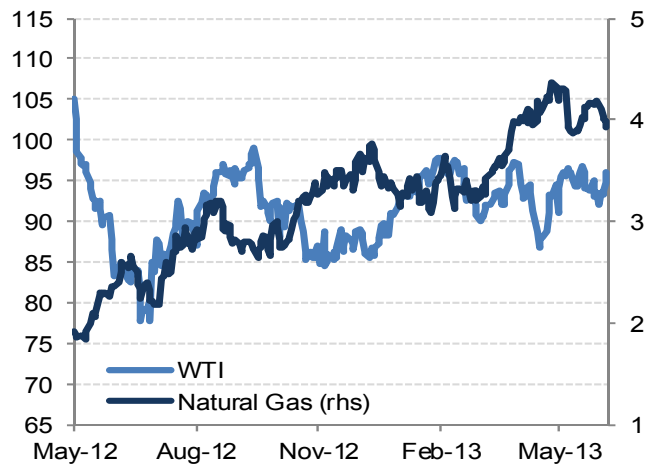
Graph 14
Total Reportable Short & Long Positions
(Short-Long, K)



Source: Haver Analytics & BBVA Research

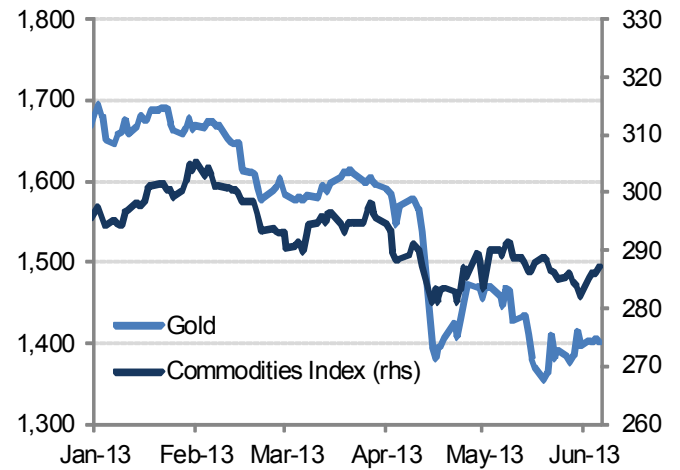
Financial Markets

Graph 15
Commodities
(Dpb & DpMMBtu)



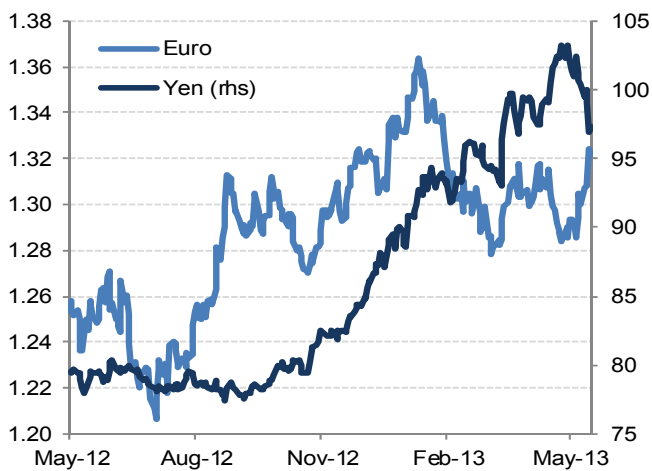
Source: Bloomberg & BBVA Research

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



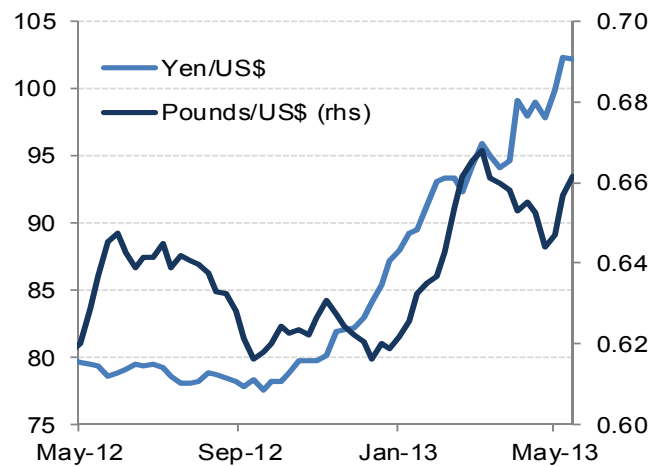
Source: Haver Analytics & BBVA Research

Graph 17
Currencies
(Dpe & Ypd)



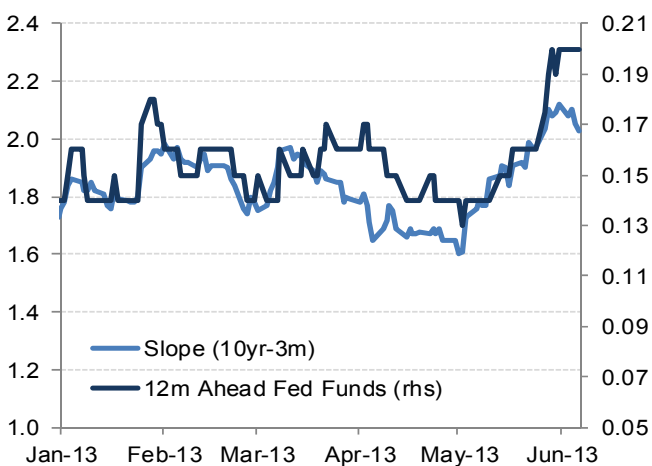
Source: Bloomberg & BBVA Research

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



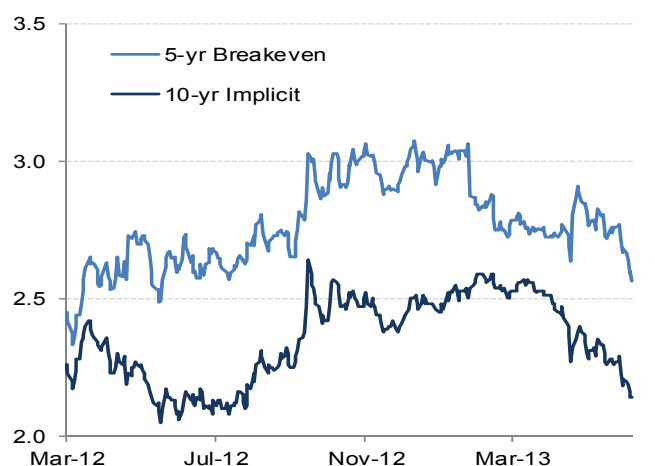
Source: Haver Analytics & BBVA Research

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	4-Weeks		
		Week ago	ago	Year ago
Prime Rate	3.25	3.25	3.25	3.25
Credit Card (variable)	14.12	14.12	14.12	14.10
New Auto (36-months)	2.47	2.46	2.30	3.07
Heloc Loan 30K	5.35	5.35	5.34	5.56
5/1 ARM*	2.74	2.68	2.56	2.90
15-year Fixed Mortgage*	3.03	2.76	2.56	3.23
30-year Fixed Mortgage*	3.91	3.57	3.35	3.99
Money Market	0.45	0.46	0.47	0.72
2-year CD	0.70	0.69	0.65	0.90

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

Table 1
Key Interest Rates (%)

	Last	4-Weeks		
		Week ago	ago	Year ago
1M Fed	0.10	0.09	0.12	0.17
3M Libor	0.28	0.27	0.45	0.47
6M Libor	0.41	0.42	0.65	0.00
12M Libor	0.69	0.68	0.98	1.07
2yr Sw ap	0.48	0.46	0.37	0.58
5yr Sw ap	1.28	1.21	0.97	1.02
10Yr Sw ap	2.35	2.30	2.04	1.82
30yr Sw ap	3.24	3.21	3.02	2.51
30day CP	0.13	0.14	0.15	0.37
60day CP	0.14	0.14	0.16	0.37
90day CP	0.17	0.17	0.17	0.34

Source: Bloomberg & BBVA Research

Quote of the Week

Dallas Federal Reserve President Richard Fisher
C.D Howe Institute Directions' Dinner
4 June 2013

"With the Arrow Caveat in mind, my staff and I think there is a better-than-even chance that the present GDP growth consensus forecast of 2.4 percent by professional economists may be underestimating the underlying pace of growth. The housing market is in resurgence, contributing significant impetus to the economy. The Fed's senior loan officer survey indicates that commercial banks are becoming more accommodative lenders, albeit remaining cautious. The snapback in housing and the harnessing of cheap and abundant money by the business sector have made for more manageable financial obligations."

Economic Calendar

Date	Event	Period	Forecast	Survey	Previous
11-Jun	Wholesale Inventories	APR	0.2%	0.2%	0.4%
13-Jun	Initial Jobless Claims	8-Jun	335K	345K	346K
13-Jun	Continued Claims	1-Jun	2970K	2975K	2952K
13-Jun	Retail Sales	MAY	0.6%	0.4%	0.1%
13-Jun	Retail Sales ex autos	MAY	0.4%	0.3%	-0.1%
14-Jun	Producer Price Index	MAY	0.1%	0.1%	-0.7%
14-Jun	PPI ex. Less Food and Energy	MAY	0.2%	0.1%	0.1%
14-Jun	Industrial Production	MAY	-0.2%	0.2%	-0.5%
14-Jun	Capacity Utilization	MAY	77.7%	77.9%	77.8%
14-Jun	Consumer Sentiment	JUN-P	85.2	84.5	84.5

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	2.0	2.2	2.3
CPI Core (YoY %)	1.7	2.1	1.9	2.0	2.1
Unemployment Rate (%)	8.9	8.1	7.5	7.0	6.5
Fed Target Rate (eop, %)	0.25	0.25	0.25	0.25	0.50
10Yr Treasury (eop, % Yield)	1.98	1.72	2.30	2.73	3.39
US Dollar/ Euro (eop)	1.32	1.31	1.29	1.30	1.35

Note: Bold numbers reflect actual data



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