

Economic Outlook

U.S. Monthly Update

July 10, 2013



Meeting Details

Topic: U.S. Monthly Economic Outlook

Date: Wednesday, July 10, 2013

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

Meeting Number / Access Code: 713 573 073

Meeting Password: bbva

To join the online meeting:

<https://bbvacompass.webex.com/bbvacompass/j.php?ED=238148147&UID=1553446432&PW=NYmJiYmM1ZjJh&RT=MiM3>

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Economic Outlook

GDP

Recovery becoming more sustainable in 2H13

- Slower than expected growth in 1Q13
- Manufacturing activity gradually picking up momentum
- Improving labor market conditions
- Solid growth in personal spending
- Strong housing recovery

Inflation

Contained pressures

- Deflationary pressures subsiding
- Core pressures from shelter and transportation
- Inflation expectations remain stable

Fed

New plan announcement

- More clarity on QE3 timeline
- Expecting faster improvements in the labor market
- Downplayed deflationary concerns

Interest Rates

Low yields for a prolonged period

- Rates only partially correct after “overreaction” to FOMC
- Fed reiterates plans for extended period of low rates
- Moderate yield curve steepening

Risks

Lower probability

- Domestic: modest fiscal concerns, QE3 costs and financial market instability, labor market weakness
- Global: deeper European crisis, slow EM, sharp change in commodity/energy prices, geopolitical threats

Economic Activity

Indicator	Assessment		Indicator	Assessment	
ISM			Unemployment Rate (%)		
ISM Non-Manufacturing			Nonfarm Payrolls (MoM Change in K)		
Capacity Utilization			Auto Sales (Millions)		
Industrial Production (YoY % Change)			Real Disposable Income (YoY % Change)		
Capital Goods New Orders (YoY % Change)			Real Personal Spending (YoY % Change)		
Housing Starts (YoY % Change)			Retail Sales Ex Auto & Gas (YoY % Change)		
Home Prices: S&P Case-Shiller (YoY % Change)			Consumer Confidence Index		

Monetary Policy Release

Economic Projections

- Moderate economic growth
- Faster decline in unemployment rate (6.5% in 2014)
- Inflation expectation remains unchanged
- Timing of first FFR hike
 - 14 of 19 FOMC members in 2015
 - 1 FOMC member in 2016

QE3

- FOMC Statement of June 19 was in line with our expectations for maintaining the current pace of (\$85bn)
- Data dependent QE3
- Moderating pace of purchases – later in 2013
- End QE3 mid 2014
- End QE3 threshold – 7% unemployment rate

Normalization

- FOMC puts out a coordinated effort of communication strategy to correct spike in long term yields
- Broad principles outlined in June 2011 still apply
- MBS will be held to maturity.

General

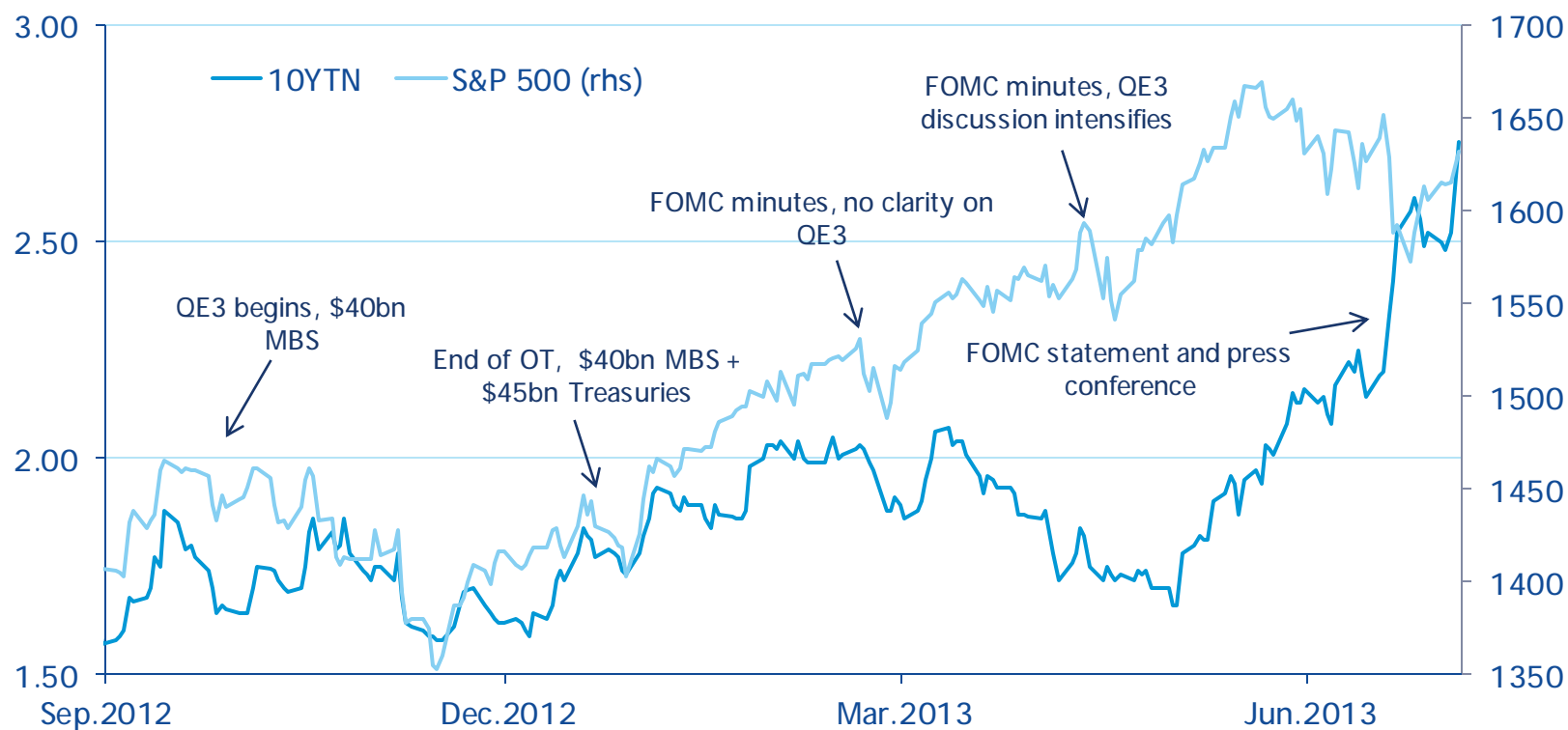
- Bernanke will step down as Chairman in 2014
- ***Dovish pull*** – reassertion of lower than expected inflation rate.
- ***Hawkish push*** – downside risks to economic growth and the labor market have “diminished since the fall” (*start of QE3*)

Financial Markets

Higher yields, drop in equities, and revisions to Fed funds expectations

10YTN & S&P500

%, Index



Two Alternative Future Paths:

Economic Fundamentals

GDP Growth

Unemployment

Inflation

Early Exit: 10%

High

Fast ↓

Moderate ↑

BBVA Baseline: 80%

Moderate

Moderate ↓

No Change

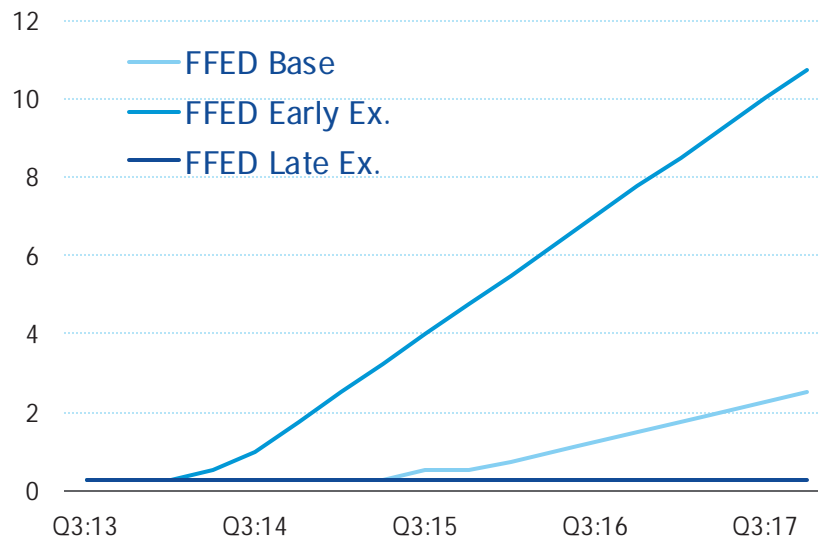
Late Exit: 10%

Low

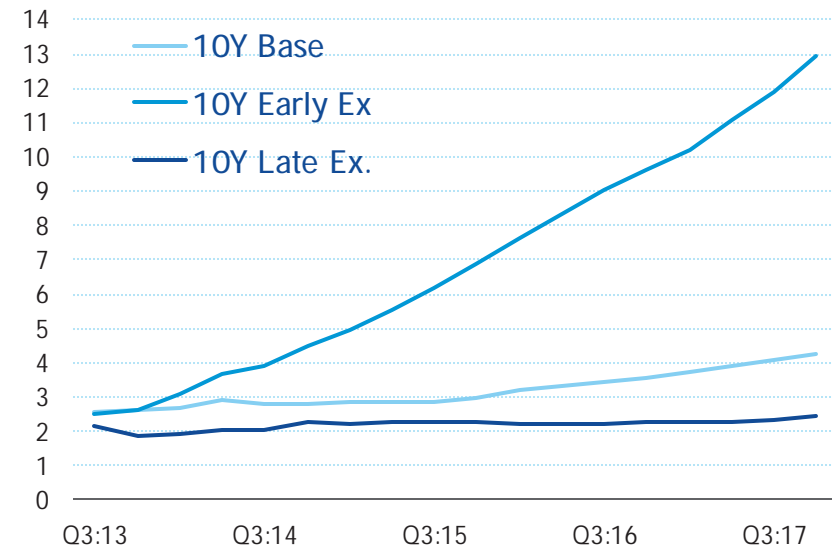
No Change

No Change

Federal Funds Rate (%)



10-Year Zero-Coupon Treasury Yield (%)



Note: Early and late exit scenarios are internal and different from the official risk scenario

QE3 and the Balance Sheet

Early Exit

- 3Q13
- 4Q13
- 2Q14
- 4Q14

BBVA Baseline

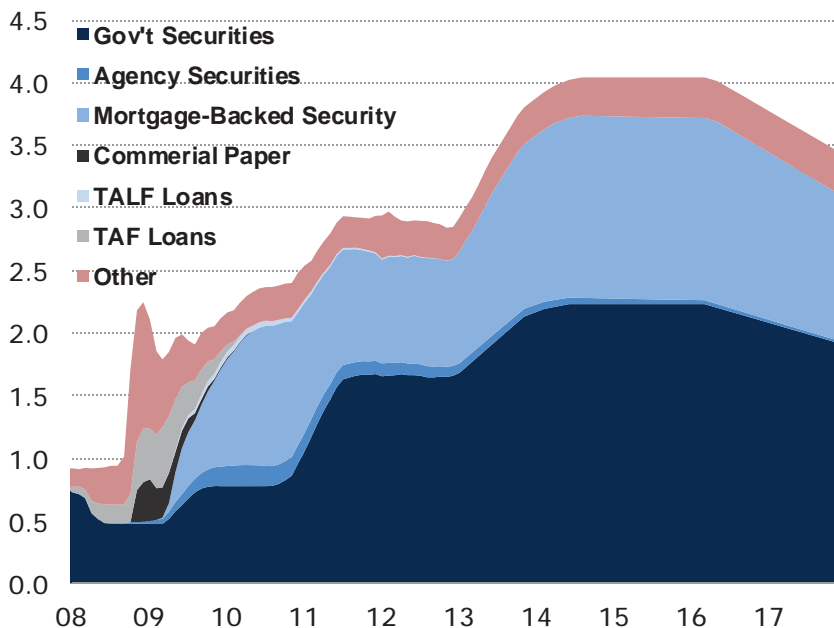
- QE3 ↓: 3Q13
- End QE3: 2Q14
- FFR ↑: 3Q15
- Exit: 2Q16

Late Exit

- 1Q15
- 4Q16
- NA
- NA

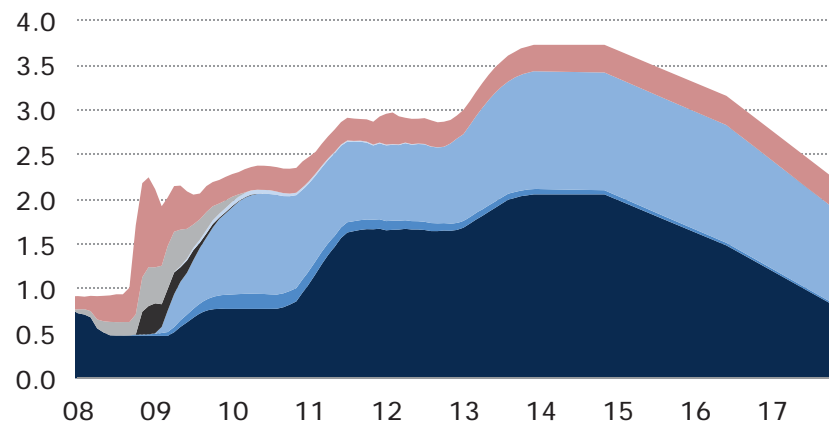
BBVA Baseline

US\$tn



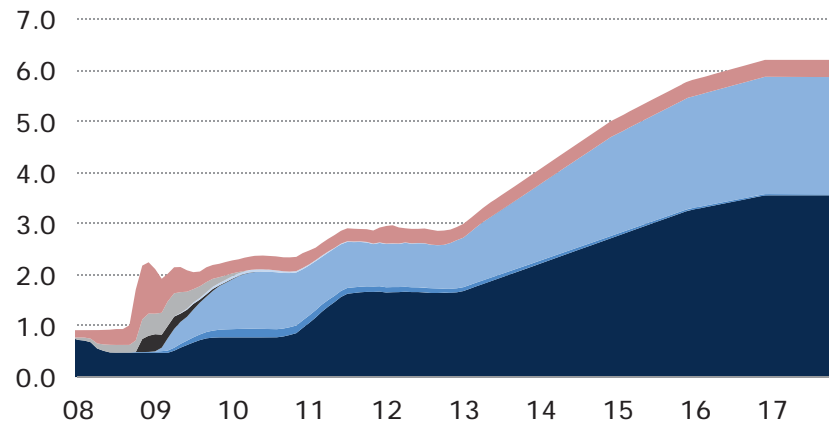
Early Exit

US\$tn



Late Exit

US\$tn



Note: Early and late exit scenarios are internal and different from the official risk scenario



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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