

Economic Outlook

U.S. Monthly Update

October 9, 2013

Meeting Details

Topic: U.S. Monthly Economic Outlook

Date: Wednesday, October 9, 2013

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

Meeting Number / Access Code: 713 344 388

Meeting Password: bbva

To join the online meeting:

<https://bbvacompass.webex.com/bbvacompass/j.php?ED=247873937&UID=1638080042&PW=NOWZiOGZiNGIz&RT=MiM3>

To join the audio conference only:

Call-in toll-free number (US/Canada): 1-877-768-4036

Call-in toll number (US/Canada): 1-972-932-2100

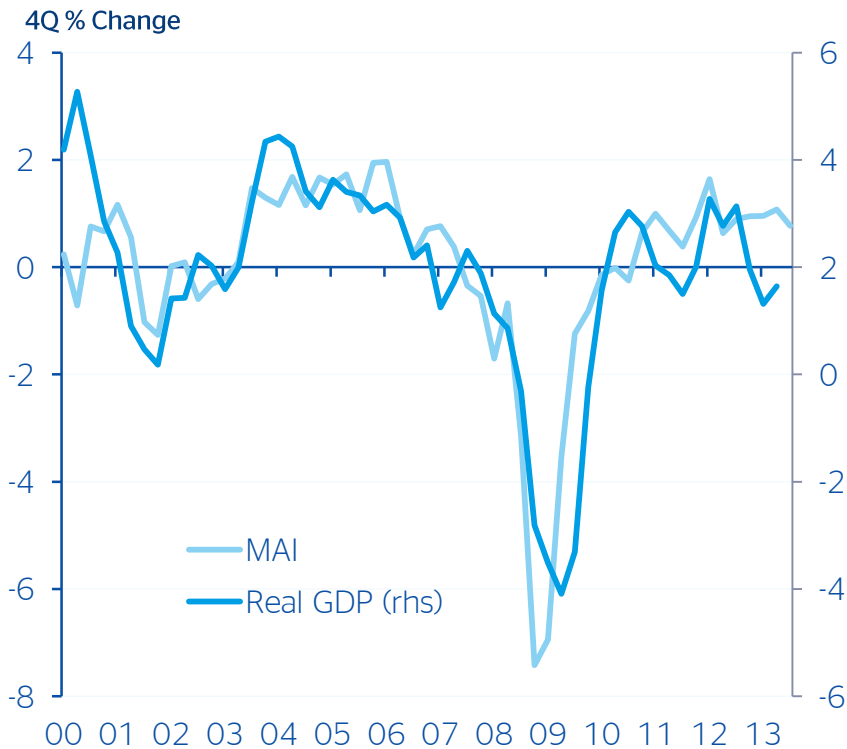
Global call-in numbers:

<https://bbvacompass.webex.com/bbvacompass/globalcallin.php?serviceType=MC&ED=187370482&tollFree=1>

Economic Activity

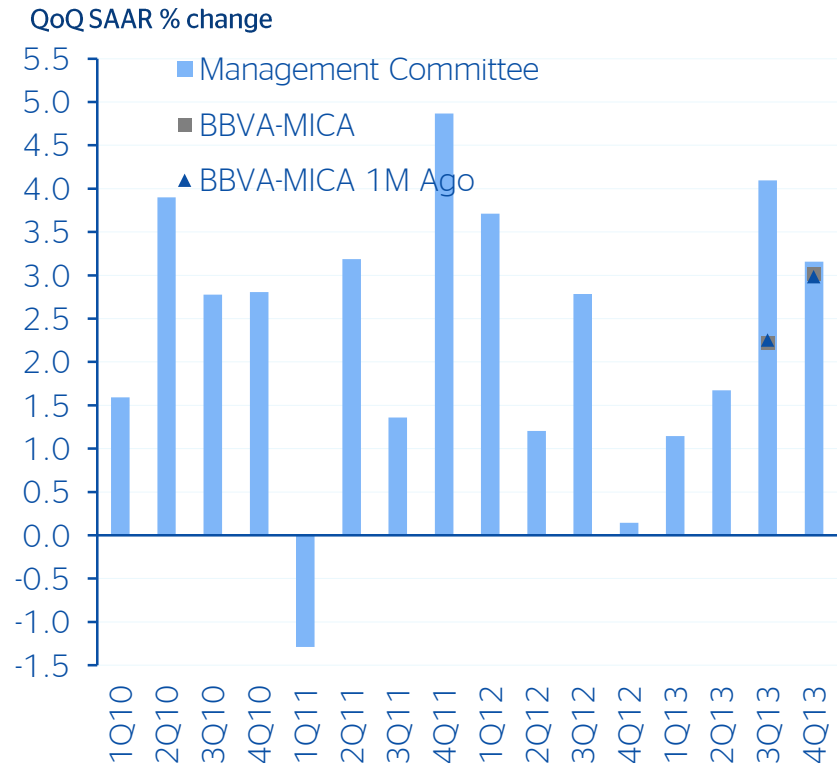
While short-term economic data have been mixed, growth will continue at 2.0-2.5% in 2H13

Real GDP & Monthly Activity Index



Source: BBVA Research

BBVA-MICA GDP Forecast



Source: BBVA Research

Economic Activity

Indicator	Assessment		Indicator	Assessment	
ISM Manufacturing			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		

U.S. Baseline Scenario

Some adjustments are likely after the next BBVA Research quarterly revision meeting

	2011	2012	2013	2014	2015	2016	2017
GDP current	1.8	2.2	1.8	2.3	2.5	2.8	2.8
previous	1.8	2.2	1.8	2.3	2.5	2.7	2.7
CPI current	3.1	2.1	1.6	2.3	2.4	2.4	2.4
previous	3.1	2.1	2.1	2.2	2.3	2.4	2.5
Core current	1.7	2.1	1.9	2.0	2.1	2.3	2.4
previous	1.7	2.1	1.9	2.0	2.1	2.3	2.4
Fed current	0.25	0.25	0.25	0.25	0.50	1.5	2.5
previous	0.25	0.25	0.25	0.25	0.50	1.5	2.5

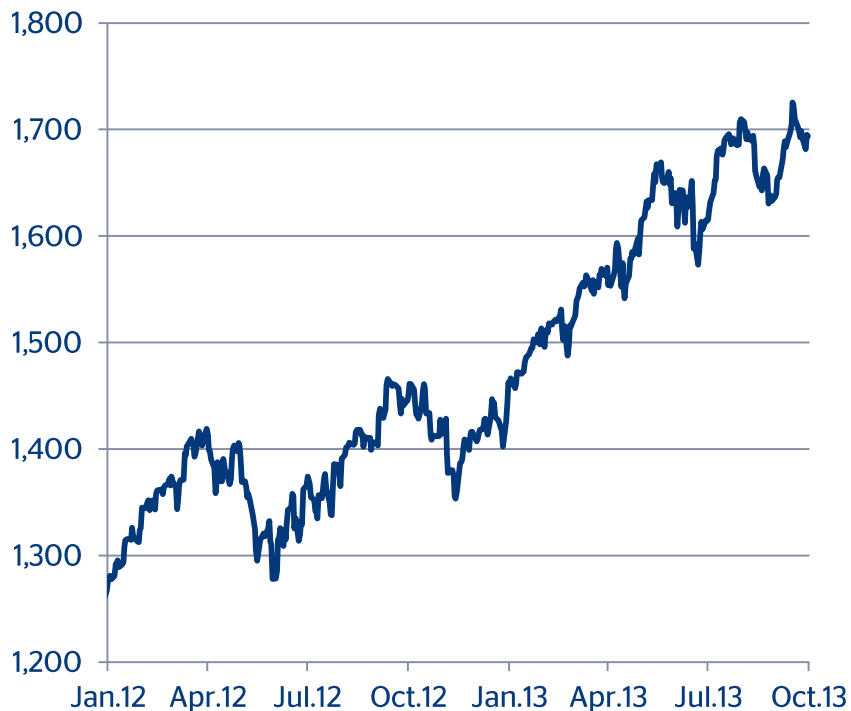
* Previous as presented in 2Q13 MC Quarterly Revision. Fed funds are end of period

Financial Markets

A strong market reaction to the FOMC decision as equities reached new highs. Limited reaction to government shutdown.

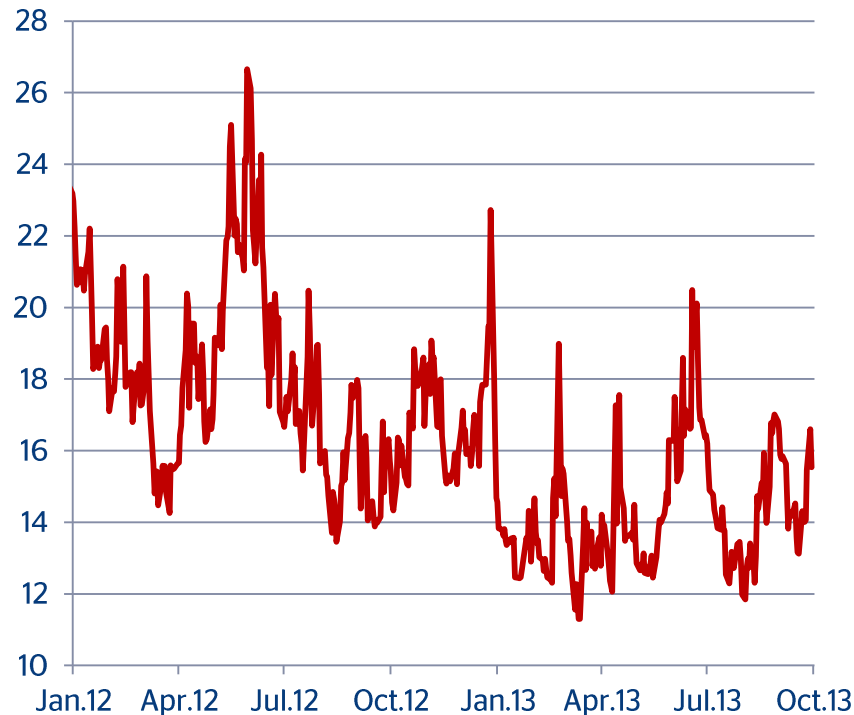
Equity Prices

S&P 500



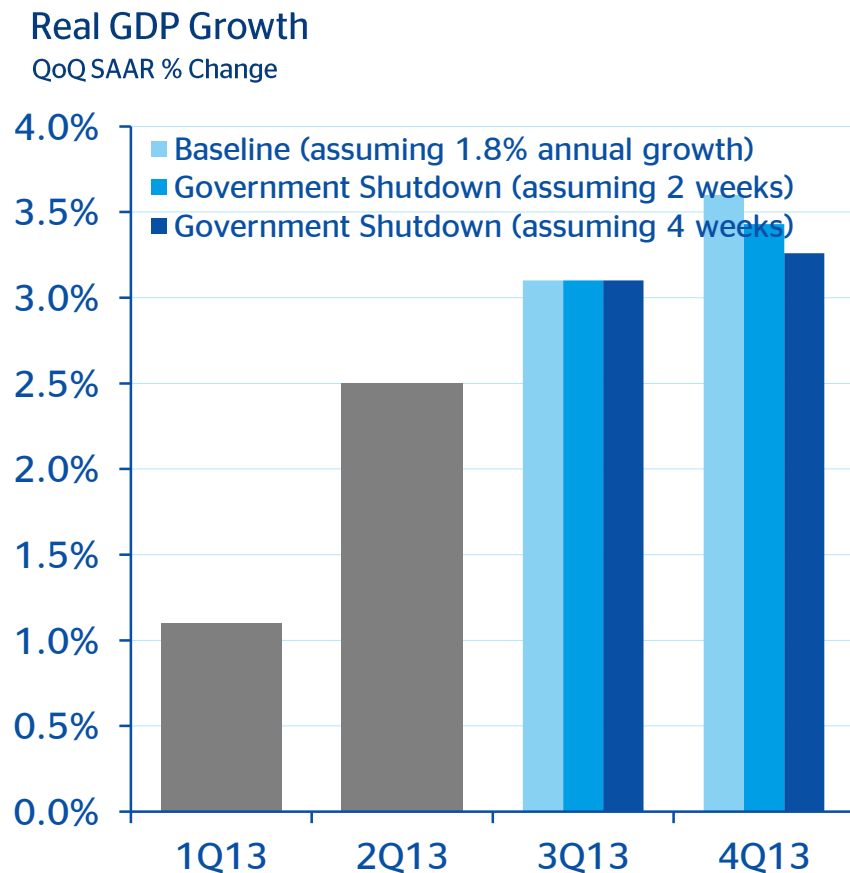
Volatility

Index



Fiscal Policy

Government shutdown poses minimal risk to 4Q13 growth if resolved soon, though longer-lasting consequences if brinkmanship persists

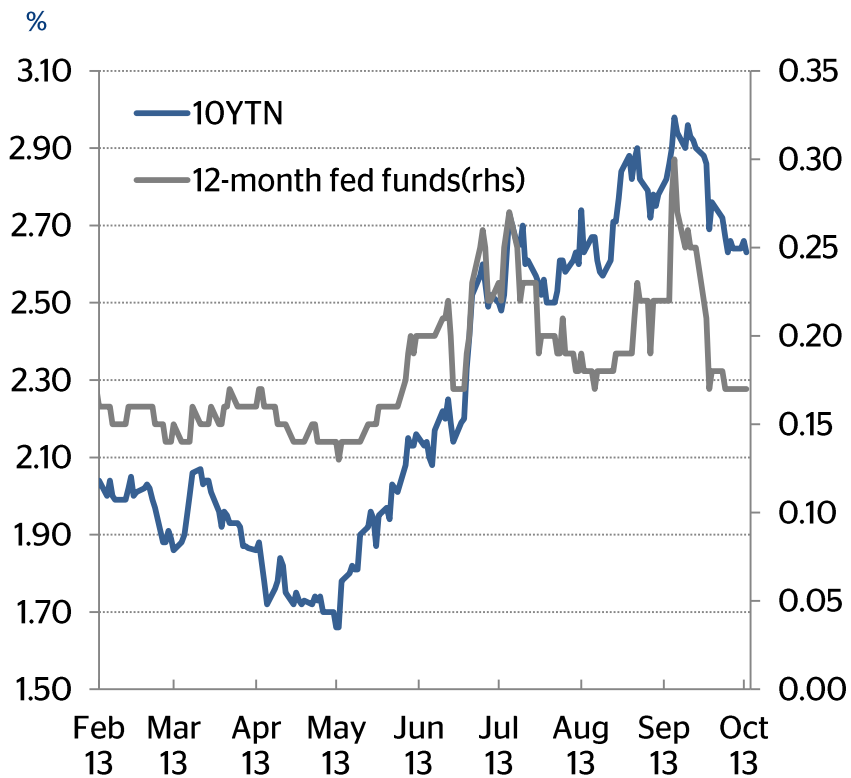


- An end to the government shutdown before debt ceiling negotiations appears unlikely
- Although public opinion is shifting towards the democrats, 2010 gerrymandering rendered many conservative congressional districts uncompetitive, reducing the Republicans incentives to compromise
- A baseline scenario assumes at-risk GOP candidates align with House Democrats, facilitating an agreement (fiscal cliff)
- Impact: -0.17% to -0.34% reduction in 4Q13 GDP QoQ SAAR growth depending on duration
- This excludes policy uncertainty shock, drop in asset prices, and offsetting Fed actions

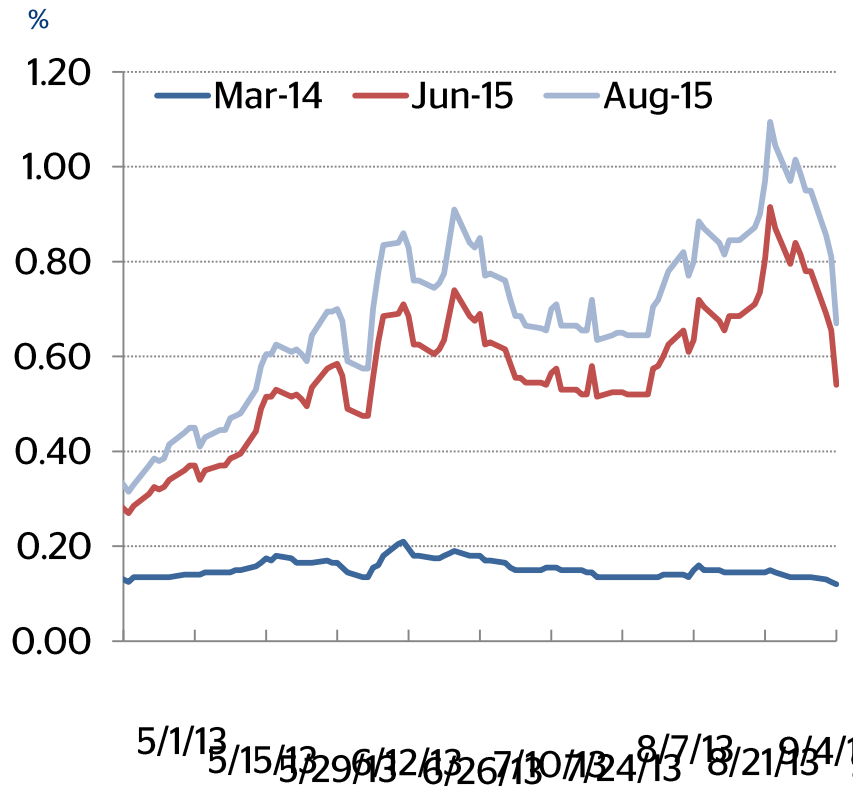
Policy Expectations

Unwinding financial positions and realigning market expectations: tapering vs. rate hike

10yTN and 12-month Fed funds futures



Fed Funds futures



FOMC September 18th Policy Decision

A surprise move by the FOMC: Doing nothing Why?

1. Insufficient labor market recovery
2. Inflation below target
3. Recent increase in interest rates can weaken the recovery
4. Unwinding financial positions and re-aligning expectations
5. Elevated risks from fiscal uncertainty

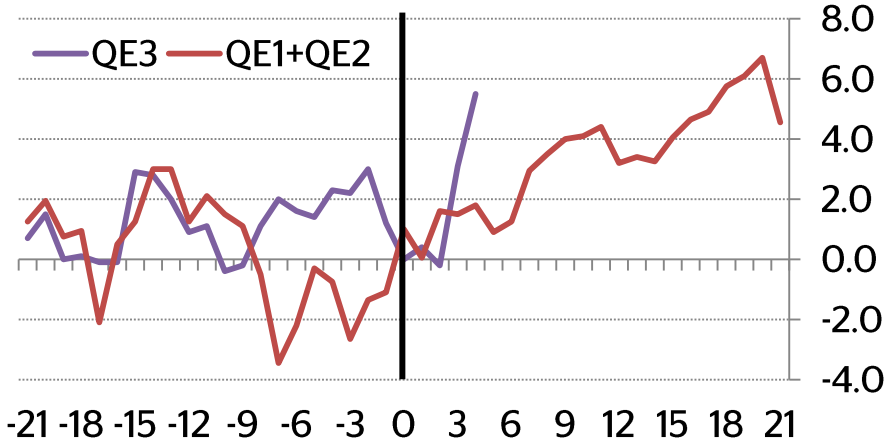
FOMC Statement September 18, 2013

“Some indicators of labor market conditions have shown further improvement in recent months, but **the unemployment rate remains elevated**. Household spending and business fixed investment advanced, and the housing sector has been strengthening, **but mortgage rates have risen further and fiscal policy is restraining economic growth**. Apart from fluctuations due to changes in energy prices, **inflation has been running below the Committee's longer-run objective**, but longer-term inflation expectations have remained stable.”

QE3 Impact

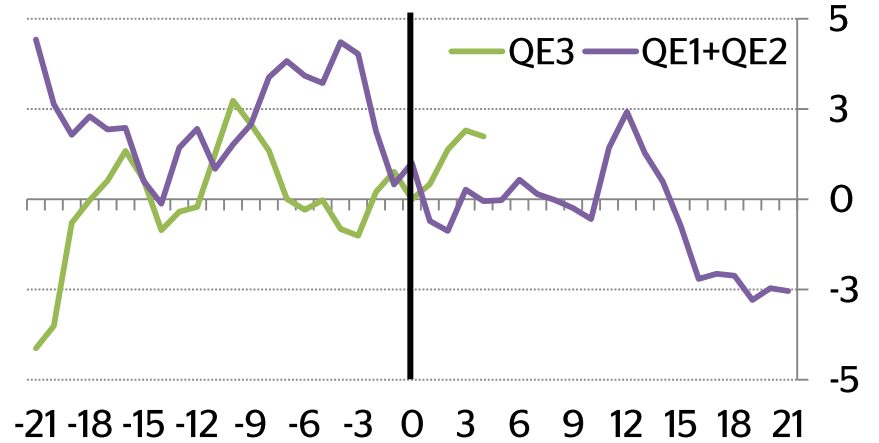
ISM

Average QE1+QE2 vs QE3, 0=start



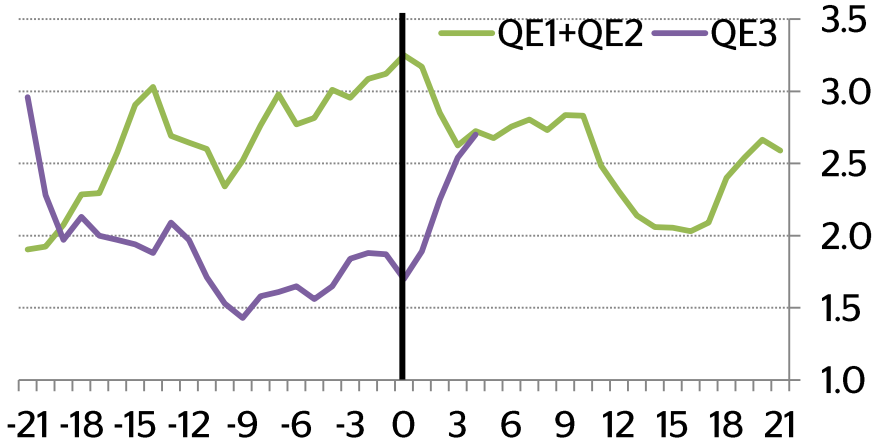
US Dollar

Average QE1+QE2 vs QE3, 0=start



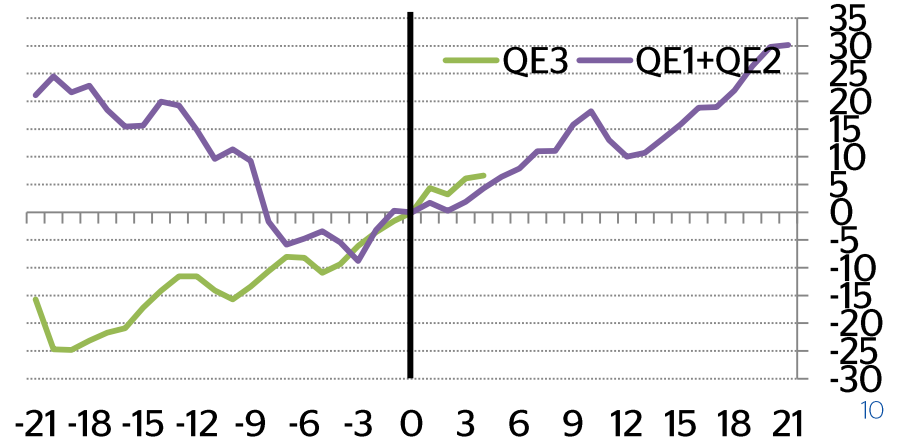
Yield Curve Slope

Average QE1+QE2 vs QE3, 0=start



S&P 500

Average QE1+QE2 vs QE3, 0=start



FOMC Economic Projections

FOMC made moderate downward revisions to the unemployment rate and GDP growth

September 2013 FOMC Projections

	2013	2014	2015	2016	Longer run
GDP, 4Q yoy % change					
Low	2.0	2.9	3.0	2.5	2.2
High	2.3	3.1	3.5	3.3	2.5
Unemployment rate, 4Q %					
Low	7.1	6.4	5.9	5.4	5.2
High	7.3	6.8	6.2	5.9	5.8
Core PCE, 4Q yoy % change					
Low	1.2	1.5	1.7	1.9	
High	1.3	1.7	2.0	2.0	

June 2013 FOMC Projections

	2013	2014	2015	2016	Longer run
GDP, 4Q yoy % change					
Low	2.3	3.0	2.9	n.a.	2.3
High	2.6	3.5	3.6		2.5
Unemployment rate, 4Q %					
Low	7.2	6.5	5.8	n.a.	5.2
High	7.3	6.8	6.2		6.0
Core PCE, 4Q yoy % change					
Low	1.2	1.5	1.7	n.a.	
High	1.3	1.8	2.0		

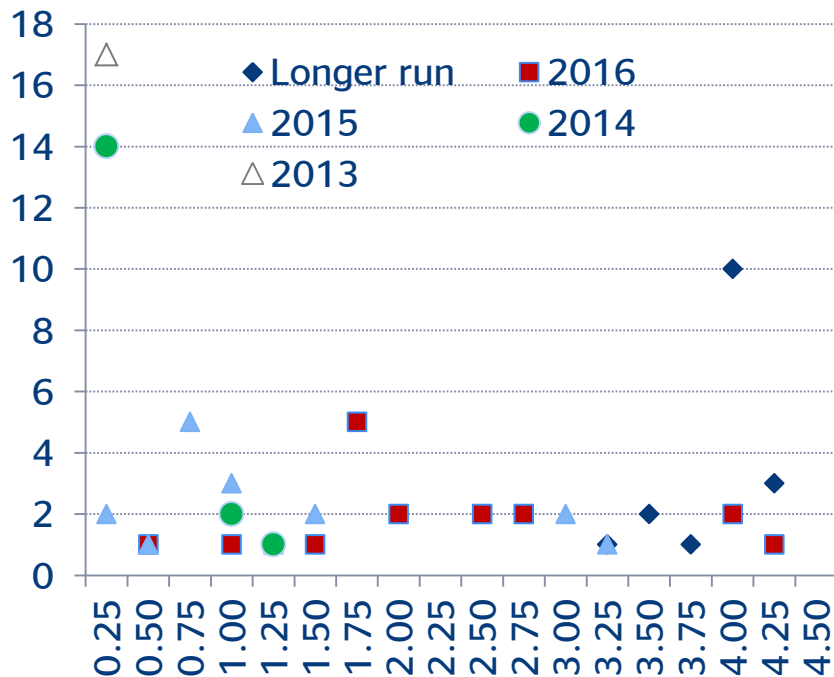
Source: Federal Reserve

FOMC Fed Funds Projections

A more dovish-leaning consensus

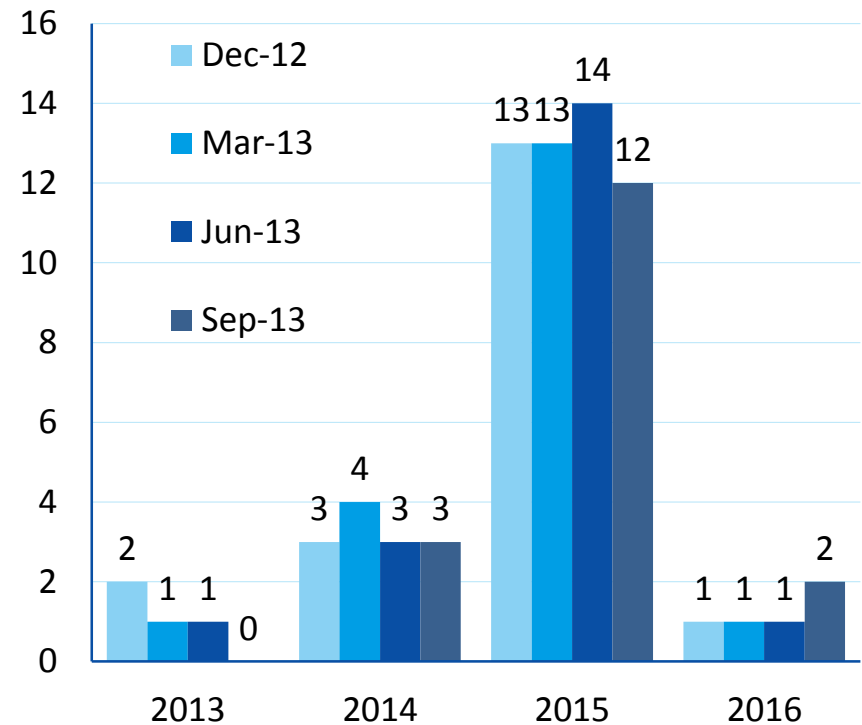
Appropriate Timing of Policy Firming

(Number of participants)



Target Federal Funds Rate Forecast

(Year-end %)



Monetary Policy Expectations

Latest

What do we expect?

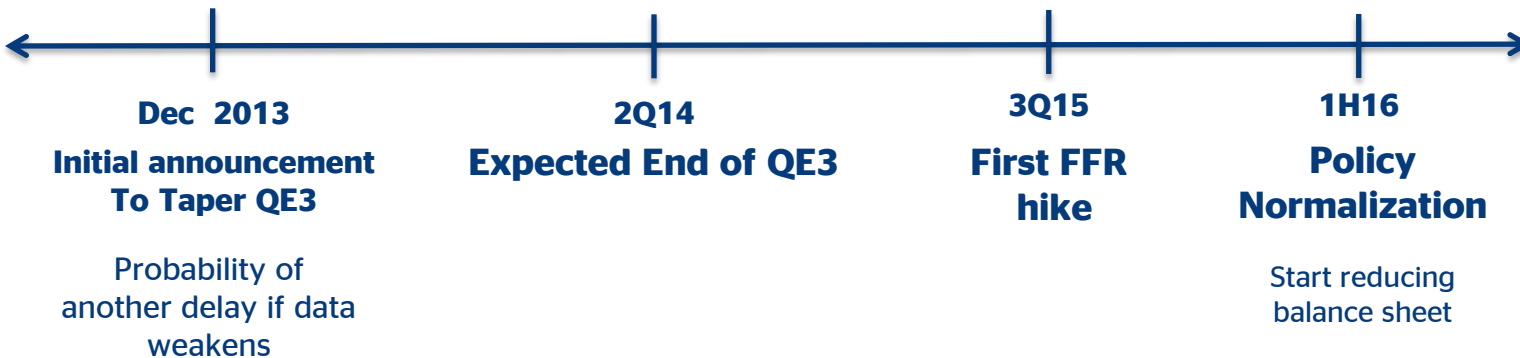
Fed

- ❖ FOMC left the \$85 billion monthly asset purchases pace unchanged
- ❖ Fed concerned with “tightening of financial conditions,” and **fiscal policy uncertainty**
- ❖ **FOMC Statement: September 18, 2013**

“Asset purchases are not on a preset course, and the Committee’s decisions about their pace will remain contingent on the Committee’s economic outlook.”

- ❖ Scaling down QE3 scenario on hold until December, at least
- ❖ QE3 remains vastly data-driven
- ❖ Delayed taper announcement can result in higher financial markets uncertainty on the expected path of QE3 and the Fed’s successful exit and policy normalization

Expected Timeline



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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