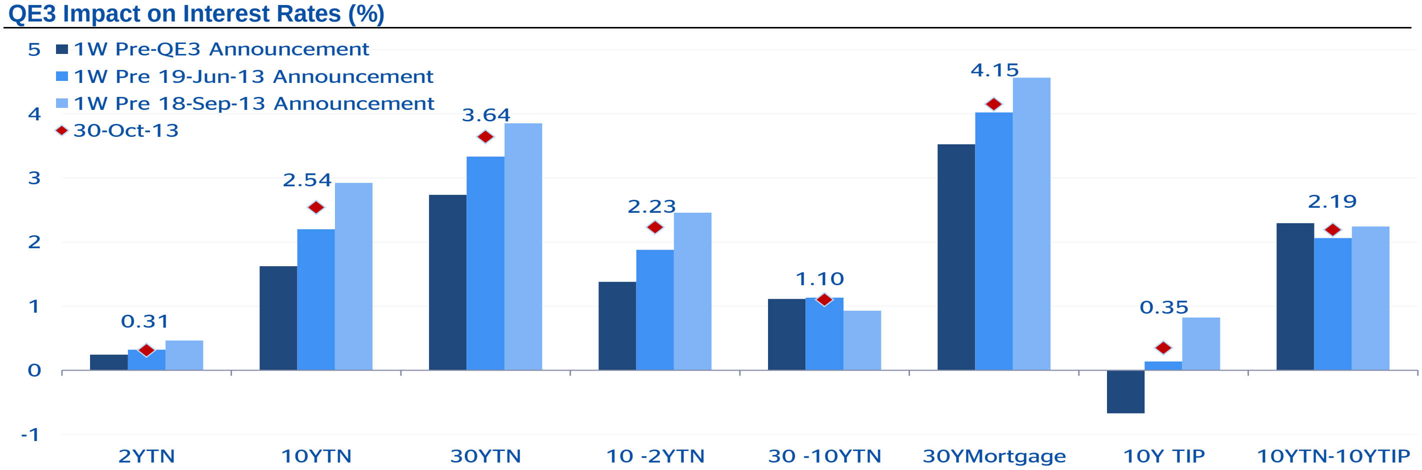
US Weekly Flash

Highlights

- **FOMC Statement: Pace of Purchases Kept Unchanged Awaiting Better Data**
  - The Fed's newly released statement did not contain any changes to the current monthly pace of the large scale asset purchases (LSAP). Subsequently, there were no changes to the forward guidance as well. The announcement took a very balanced stance and, while giving in to the dovish market expectations to keep monthly purchases unchanged, it contained slight hawkish undertones of continued optimism regarding the overall economic outlook. The statement did not reflect any negativity on third and fourth quarter growth prospects in connection with the recent government shutdown and congressional brinkmanship. However, the FOMC remains concerned over low inflation rates, restating that it "recognizes that inflation persistently below its 2 percent objective could pose risks to economic performance." The delayed September CPI estimates indicated that both headline and core CPI measures of inflation remain low, with headline CPI at 1.2% YoY and core CPI at 1.7%. PCE inflation measures are also below the 2% mark.
  - Overall, the FOMC statement was balanced and carefully crafted not to communicate either dovish or hawkish expectations to the public and the markets. The Committee once again confirmed that the monthly pace of LSAP will remain data driven. A December announcement to scale down the pace of asset purchases remains contingent upon a strong revision of September employment indicators as well as sustainable economic and labor market progress in October.
- **Delayed Data Paint a Hazy Picture for September**
  - Industrial production for September was better than expected, but only at face value, up 0.6% for the month. However, much of this was due to a sharp 4.4% gain in utilities output (most likely related to the changing weather). Manufacturing production, which is a more important indicator when it comes to assessing business and consumer demand, increased only 0.1% after a downwardly revised 0.5% gain in August.
  - Similarly, retail sales for September painted a somewhat misleading picture, with the headline figure down 0.1% but the ex-auto number up 0.4%. Seasonal issues are partially to blame when it comes to auto sales, which fell 2.2% for the month and also decelerated on a YoY basis to a 12-month low of 5.1%. Overall, consumer activity in 3Q13 doesn't appear to have improved much from 2Q13.
  - On a brighter note, the ISM Manufacturing Index increased slightly to 56.4 in October, with new orders and production holding near recovery highs. The index for new export orders jumped to the highest level seen in more than a year, suggesting that the worst of the global slowdown is over. While other manufacturing indicators have not been as positive, the ISM index clearly points to healthy growth in the sector, particularly during this vulnerable period of high fiscal and monetary policy uncertainty.

Graph 1
QE3 Impact on Interest Rates (%)



Source: Federal Reserve & BBVA Research

Week Ahead

ISM Non-Manufacturing Index (October, Tuesday 10:00 ET)

Forecast: 53.7	Consensus: 54.0	Previous: 54.4

The ISM Non-Manufacturing Index is expected to decline again in October for the second consecutive month as the government shutdown and other headwinds weigh temporarily on business activity. In September, the index suggested that activity in the services sector decelerated at the fastest pace since the crisis, but still remained above the expansionary threshold. The three major components of the index (business activity, new orders, and employment), all dropped in September and point to another modest reading for October. In particular, the decline in the new orders index suggests that future activity will remain subdued until businesses and consumers regain confidence in the economy.

GDP, Advance Estimate (3Q13, Thursday 8:30 ET)

Forecast: 2.3%	Consensus: 2.0%	Previous: 2.5%

Real GDP growth has been quite sluggish throughout the past few quarters as both domestic and global headwinds linger. In 2Q13, we saw a relatively strong growth rate coming off a very low 4Q12 and 1Q13, despite the fact that underlying economic data were not so encouraging. For 3Q13, we have limited data available as the government shutdown caused a significant delay in economic releases. However, from what we can see, the quarter did not get off to a great start. Real personal consumption is on track to almost match 2Q13's figure, but hesitant consumer spending leading up to the government shutdown most likely limited growth for the end of 3Q13. Export growth declined in both July and August, while import growth was mostly subdued. Private investment and business inventory growth were also soft for the first part of the third quarter. Based on these less optimistic expectations for 2H13 growth, we revised down our real GDP forecast from 1.8% to 1.6% for 2013.

Nonfarm Payrolls and Unemployment Rate (October, Friday 8:30 ET)

Forecast: 135K, 7.2%	Consensus: 125K, 7.3%	Previous: 148K, 7.2%

Employment growth was anything but encouraging in September, and the outlook for October is no better. The government shutdown is obviously the big factor for the month, weighing on total nonfarm payroll growth. Government payrolls actually increased in August and September, while private payrolls decelerated rather significantly, falling farther from the 200K mark. Aside from the shutdown, other sectors most likely stepped back from hiring in October, particularly manufacturing. Various regional surveys for the month suggest that manufacturers reduced the rate of hiring but increased employee hours. Furthermore, temporary help has been on the rise as many employers adjust to the new healthcare laws in place, especially for small businesses. Despite this discouraging job growth, the unemployment rate continues to fall, but we expect that this trend will slow in the next few quarters as the employment outlook improves and more people re-enter the workforce.

Personal Income and Outlays (September, Friday 8:30 ET)

Forecast: 0.1%, 0.1%	Consensus: 0.3%, 0.2%	Previous: 0.4%, 0.3%

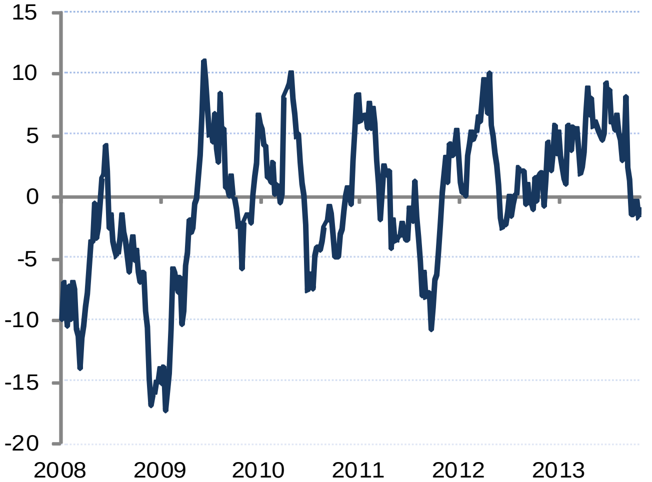
Personal income and consumption have held steady at relatively stable growth rates throughout the past few months, yet we have not seen significant acceleration worthy of a stronger recovery. On the income side, wage growth remains subdued given excess resource slack and the overall weak state of the labor market. In September, the disappointing employment report noted only modest growth in average hourly earnings, which will also most likely translate into lower consumer spending for the month. Other consumption indicators for September, such as retail sales, do not point to a strong month for consumer demand. In general, we expect the personal income and outlays report to close out 3Q13 on a humble note, with the hopes that the holiday shopping season will bring on stronger data for the end of the year.

Market Impact

This week we will finally have a clearer picture of economic activity in 3Q13 with the advance release of the GDP report and other details in the personal income and outlays data. So far, the data has not pointed to signs of immediate Fed tapering, which the FOMC confirmed in their latest statement. This should keep markets relatively quiet and happy for the week, unless we see a surprise to the downside when it comes to the GDP figure. Expectations are already quite low for October's employment report on Friday, so only a really depressed number will shock markets before the long holiday weekend.

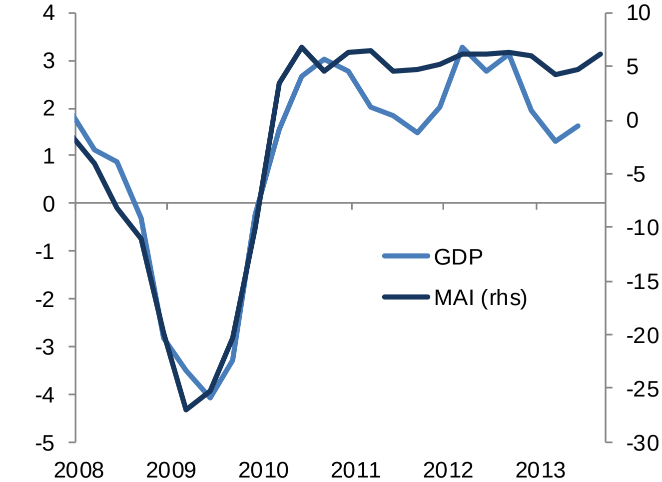
Economic Trends

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



Source: BBVA Research

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

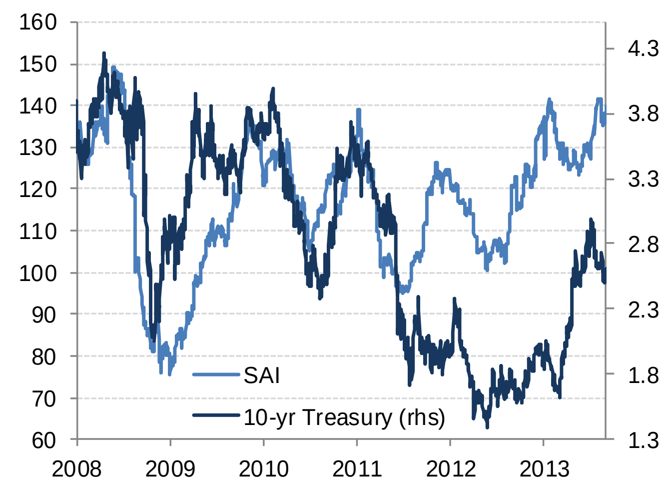


Source: BBVA Research & BEA

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

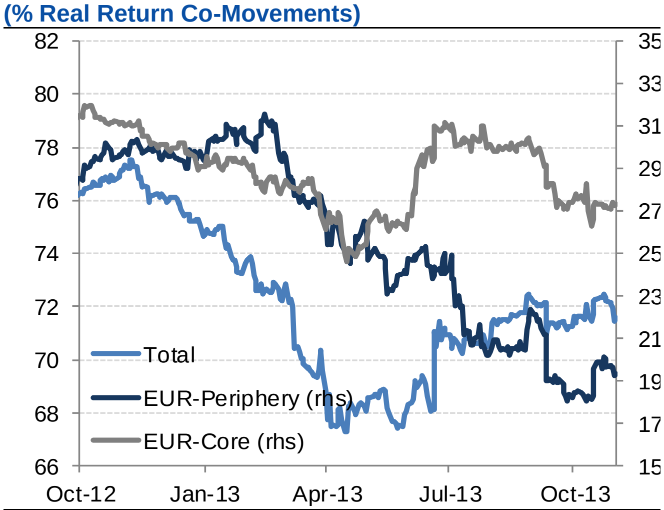
Source: BBVA Research

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



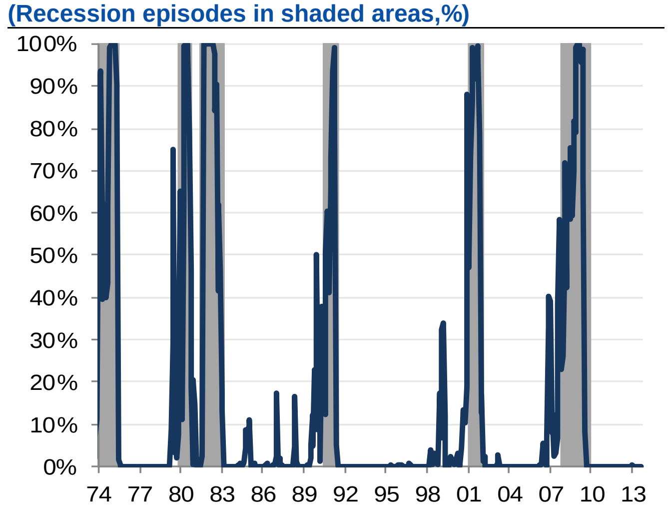
Source: Bloomberg & BBVA Research

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



Source: BBVA Research

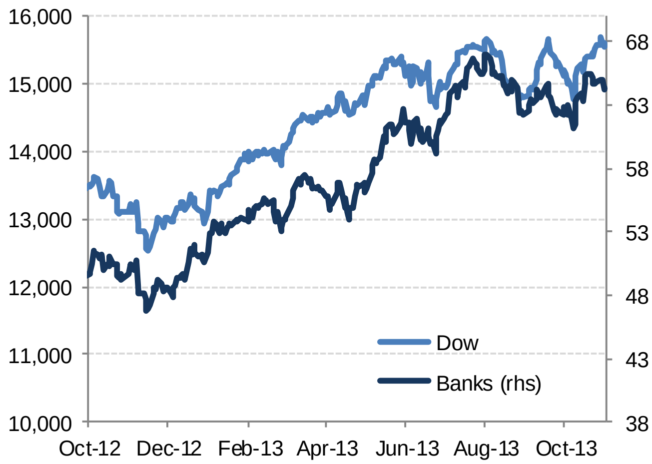
Graph 8
BBVA US Recession Probability Model
(Recession episodes in shaded areas,%)



Source: BBVA Research

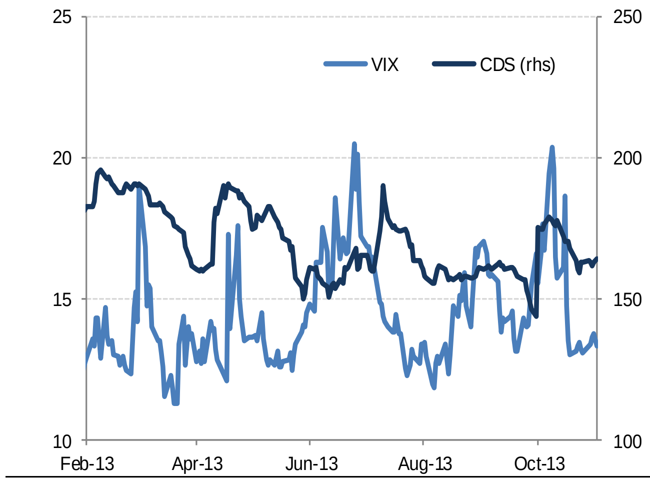
Financial Markets

Graph 9
Stocks
(Index, KBW)



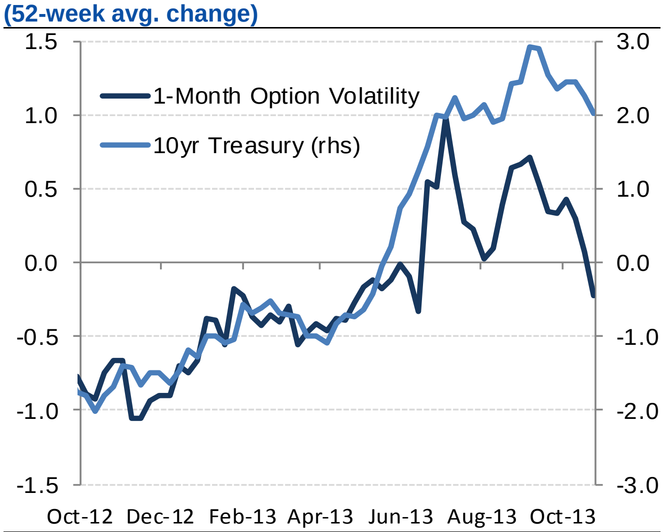
Source: Bloomberg & BBVA Research

Graph 10
Volatility & High-Volatility CDS
(Indices)



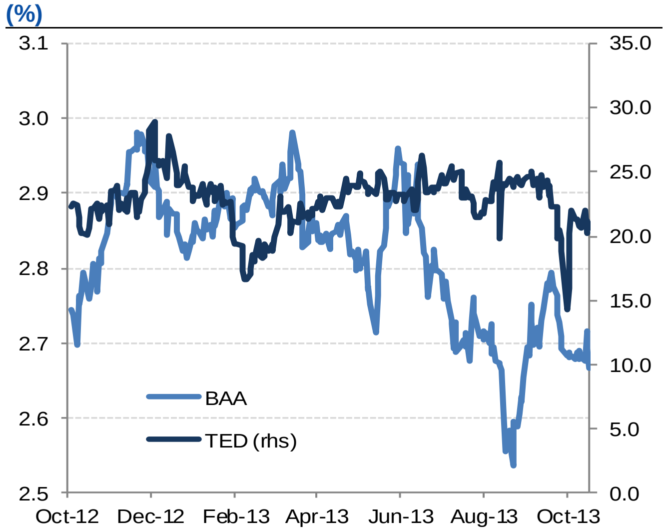
Source: Bloomberg & BBVA Research

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



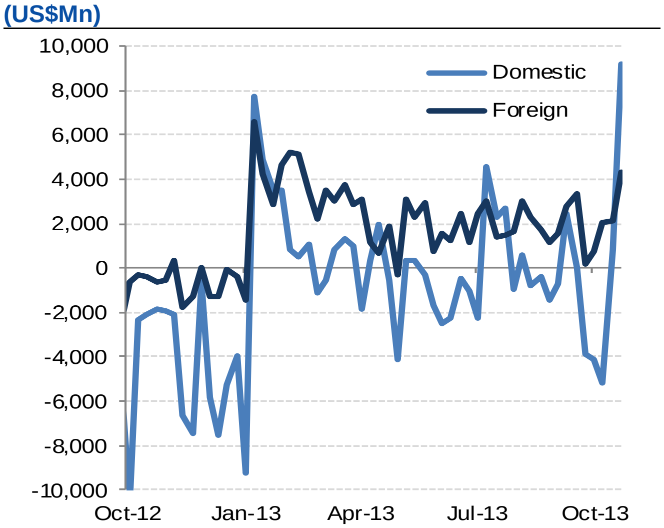
Source: Haver Analytics & BBVA Research

Graph 12
TED & BAA Spreads
(%)



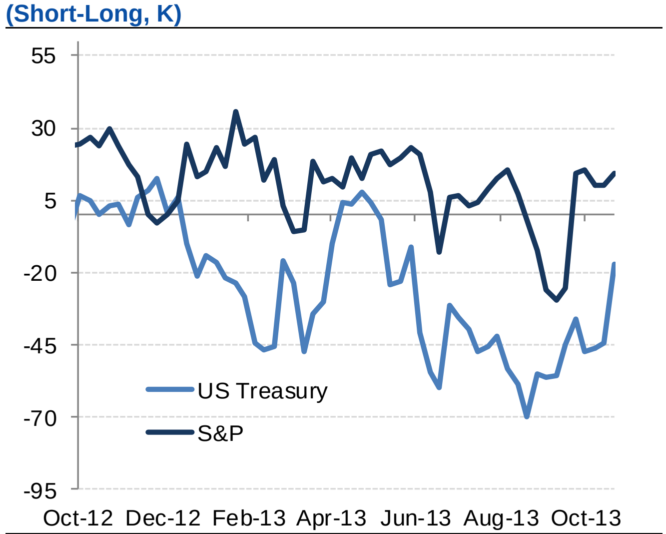
Source: Bloomberg & BBVA Research

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



Source: Haver Analytics & BBVA Research

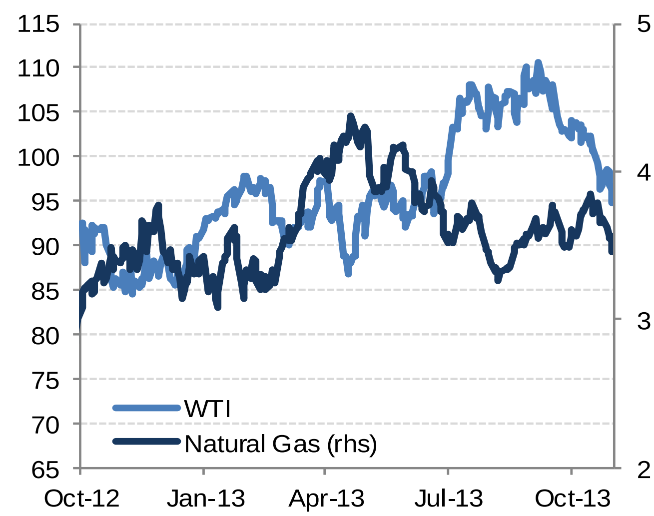
Graph 14
Total Reportable Short & Long Positions
(Short-Long, K)



Source: Haver Analytics & BBVA Research

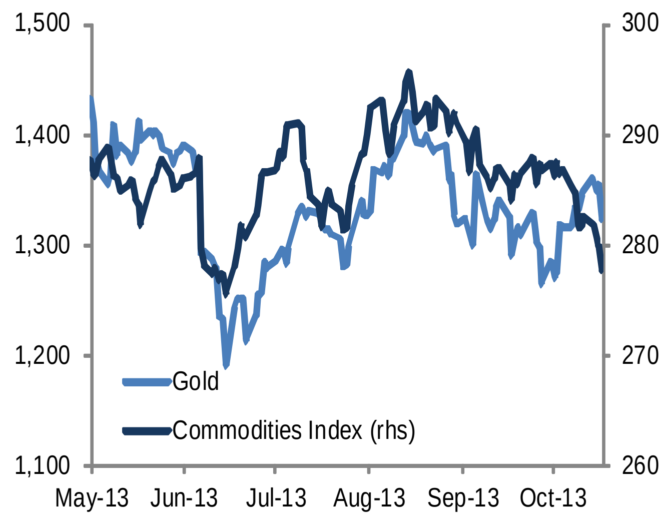
Financial Markets

Graph 15
Commodities
(Dpb & DpMMBtu)



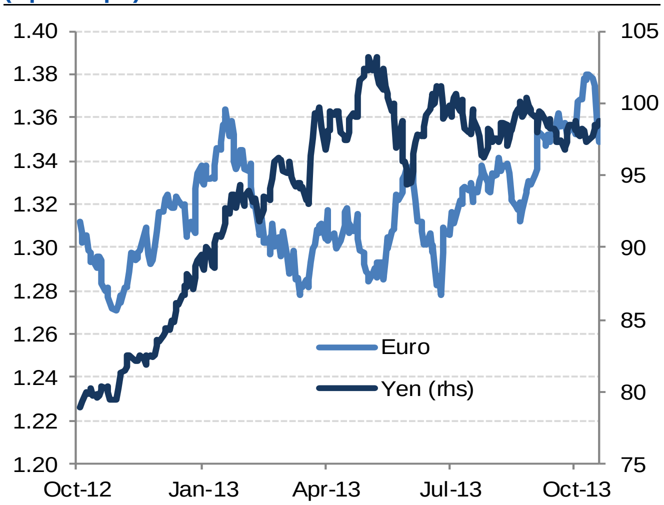
Source: Bloomberg & BBVA Research

Graph 16
Gold & Commodities
(US$ & Index)



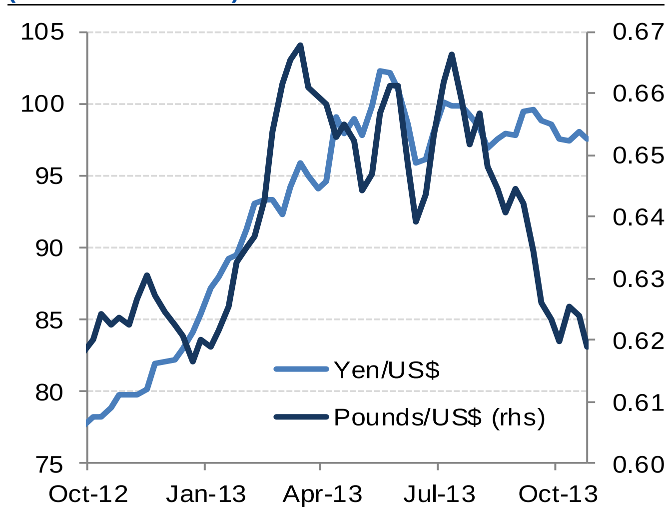
Source: Haver Analytics & BBVA Research

Graph 17
Currencies
(Dpe & Ypd)



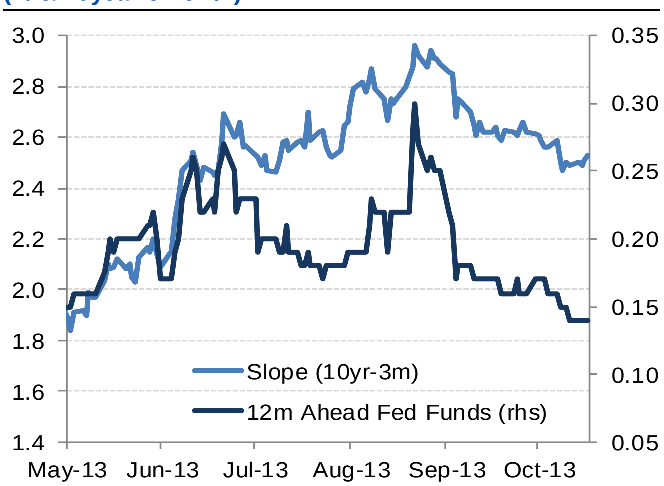
Source: Bloomberg & BBVA Research

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



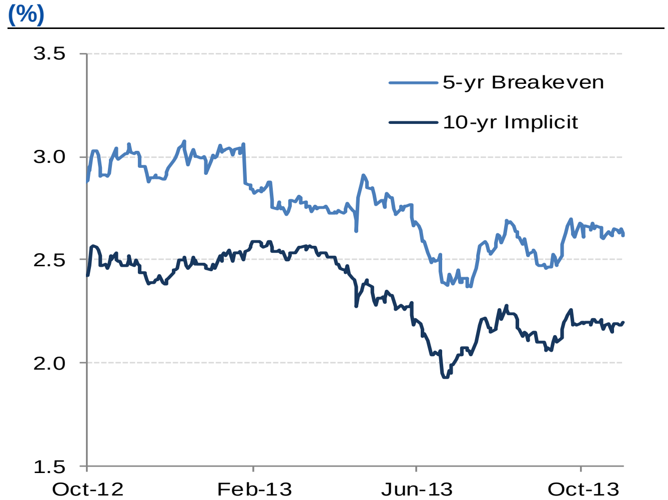
Source: Haver Analytics & BBVA Research

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	Week ago	4-Weeks ago	Year ago
Prime Rate	3.25	3.25	3.25	3.25
Credit Card (variable)	14.16	14.16	14.16	14.10
New Auto (36-months)	2.64	2.63	2.49	3.13
Heloc Loan 30K	5.26	5.26	5.20	5.45
5/1 ARM *	2.96	3.00	3.03	2.90
15-year Fixed Mortgage *	3.20	3.24	3.29	3.23
30-year Fixed Mortgage *	4.10	4.13	4.22	3.99
Money Market	0.42	0.42	0.41	0.51
2-year CD	0.81	0.81	0.80	0.84

*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	0.07	0.08	0.08	0.16
3M Libor	0.24	0.24	0.24	0.31
6M Libor	0.35	0.36	0.37	0.54
12M Libor	0.60	0.61	0.62	0.88
2yr Sw ap	0.43	0.43	0.46	0.38
5yr Sw ap	1.51	1.44	1.57	0.84
10Yr Sw ap	2.77	2.66	2.81	1.77
30yr Sw ap	3.67	3.58	3.70	2.64
30day CP	0.10	0.12	0.10	0.20
60day CP	0.11	0.15	0.11	0.21
90day CP	0.13	0.15	0.14	0.22

Source: Bloomberg & BBVA Research

Quote of the Week

James Bullard, President of the Federal Reserve Bank of St. Louis
Data Dependency of Tapering and Current Policy Tools
1 November 2013

“I would like to see inflation coming back toward target before we make a decision to taper. I would not want to speculate on what the committee will do in December. I have been an advocate that we keep our options open at every meeting.”

Economic Calendar

Date	Event	Period	Forecast	Survey	Previous
4-Nov	Factory Orders (MoM)	AUG	0.50%	0.30%	-2.75%
4-Nov	Factory Orders (MoM)	SEPT	2.10%	1.80%	--
5-Nov	ISM Non-Manufacturing Index	OCT	53.70	54.00	54.40
7-Nov	GDP QoQ Annualized	3Q A	2.3%	2.0%	2.5%
7-Nov	Personal Consumption	3Q A	1.6%	1.6%	1.8%
7-Nov	GDP Price Index	3Q A	1.4%	1.4%	0.6%
7-Nov	Core PCE QoQ	3Q A	1.6%	1.5%	0.6%
7-Nov	Initial Jobless Claims	2-Nov	331K	335K	340K
7-Nov	Continuing Claims	26-Oct	2850K	2879K	2881K
7-Nov	Consumer Credit	SEPT	$9.90B	$12.20B	$13.63B
8-Nov	Nonfarm Payrolls	OCT	135K	125K	148K
8-Nov	Private Payrolls	OCT	150K	130K	126K
8-Nov	Manufacturing Payrolls	OCT	1K	5K	2K
8-Nov	Unemployment Rate	OCT	7.2%	7.3%	7.2%
8-Nov	Average Hourly Earnings (MoM)	OCT	0.10%	0.20%	0.10%
8-Nov	Personal Income (MoM)	SEPT	0.1%	0.3%	0.4%
8-Nov	Personal Spending (MoM)	SEPT	0.1%	0.2%	0.3%
8-Nov	U. of Michigan Consumer Sentiment	OCT	74.0	74.5	73.2

Forecasts

	2011	2012	2013	2014	2015	2016
Real GDP (% SAAR)	**1.8**	**2.8**	1.6	2.3	2.5	2.8
CPI (YoY %)	**3.1**	**2.1**	1.7	2.2	2.4	2.4
CPI Core (YoY %)	**1.7**	**2.1**	1.8	2.0	2.1	2.3
Unemployment Rate (%)	**8.9**	**8.1**	7.5	7.0	6.4	5.9
Fed Target Rate (eop, %)	**0.25**	**0.25**	0.25	0.25	0.50	1.50
10Yr Treasury (eop, % Yield)	**1.98**	**1.72**	2.90	3.37	3.64	4.05
US Dollar/ Euro (eop)	**1.31**	**1.31**	1.30	1.30	1.38	1.36

Note: Bold numbers reflect actual data

Kim Fraser
Kim.Fraser@bbvacompass.com

BBVA | RESEARCH

| 2200 Post Oak Blvd, 21st Floor, Houston, Texas 77056 | Tel.: +1 713 831 7345 | www.bbvaresearch.com