

# Economic Watch

US

Houston, January 9, 2014  
Economic Analysis

## Monthly US Outlook: January New Year Commands More Optimistic Economic Views

US

Kim Fraser  
kim.fraser@bbvacompass.com

- A positive end to 2013 with improving economic data and a fiscal deal
- Tapering, Yellen, and guidance set 2014 to be a big year for the Fed
- Upward bias to GDP growth in 2014 with diminishing downside risks

As we step foot into the New Year, it's time to sit back and reflect on where we've come from in the economic recovery and where we are heading in 2014. There were plenty of ups and downs throughout 2013, mostly related to monetary and fiscal policy changes and expectations. With the recent two-year budget agreement in Congress, fiscal policy uncertainty will likely fall to the background (at least temporarily), bringing the Fed's highly accommodative monetary policy stance to center stage. At the same time, we are seeing clearer improvement in economic data, including employment growth and confidence measures that encourage a brighter outlook for 2014. GDP growth has also been stronger-than-expected in the latter half of 2013, with the 3Q13 final estimate revised up to 4.1% QoQ SAAR and much of the momentum appearing to carry over into the fourth quarter. Consequently, we are likely to see annual growth around 1.8% for 2013.

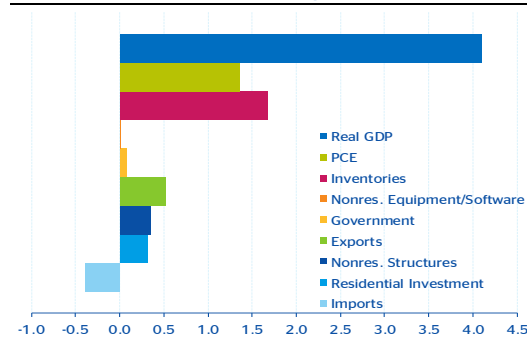
Looking forward, 2014 is shaping up to be relatively strong compared to 2013 as risks shift more to the upside. Downside risks have surely diminished, particularly on the fiscal side - the two-year budget agreement prevents some of the automatic spending cuts planned in the sequester, ultimately creating less of a drag on growth for the year. While there are definitely lingering political issues to face in 2014 (i.e. the debt ceiling limit, House elections, etc), reduced fiscal uncertainty should help boost overall economic confidence. This alone has lifted our GDP forecast for the year to 2.5%.

When it comes to the Fed, 2014 could be an exciting year. Tapering has officially begun, and we expect that the process will continue in "measured steps" of around \$10bn per month, split evenly between MBS and Treasuries, with QE3 finally coming to an end in 4Q14. This does not change our expectations for the Fed Funds Rate, with the first hike expected in 3Q15 (see [Fedwatch](#)). Janet Yellen, the new chairwoman, is expected to uphold consistency in the Fed's strategy as laid out by Bernanke throughout the past few years. Overall, the biggest challenge for the Fed is to assure a smooth transition in implementing an exit strategy, as there is some uncertainty related to the eventual normalization process. However, with the slow tapering process taking us through most of 2014, the downside Fed-related risks for this year are limited.

As incoming economic data continue to show signs of improvement, upside risks to growth are materializing. Financial market confidence has been building for some time now, and consumer and business sentiments are finally starting to catch up. Consistent improvement in economic reports will further the boost in confidence and could add a few percentage points to our existing 2014 GDP forecast of 2.5%. Similarly, this could spill over to a faster pickup in global growth, further lifting our GDP forecast via an improvement in demand for U.S. exports. While these upside scenarios seem more plausible now compared to six months ago, major contributors to growth are still running below comparable pace from prior expansions.

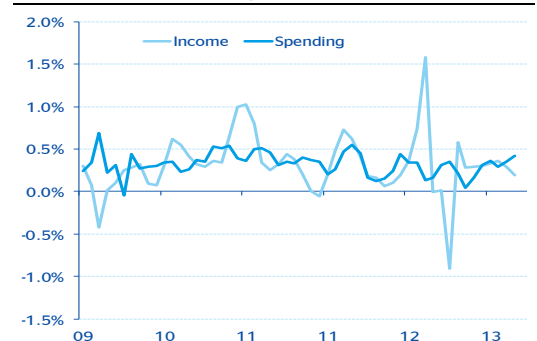
## Economic Indicators

**Graph 1**  
Contributions to Real GDP Growth  
(3Q13 Final, SAAR Percentage Points)



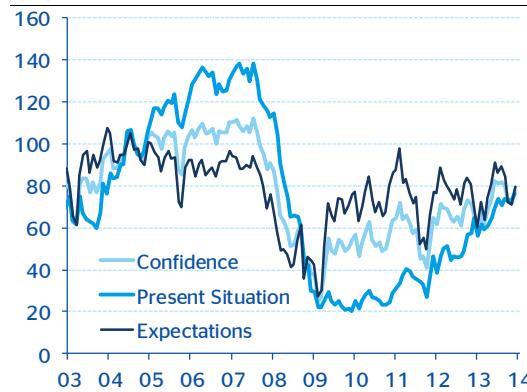
Source: BEA and BBVA Research

**Graph 2**  
Personal Income and Expenditures  
(3MMA, MoM % Change)



Source: BEA and BBVA Research

**Graph 3**  
Consumer Confidence  
(SA, Index 1985=100)



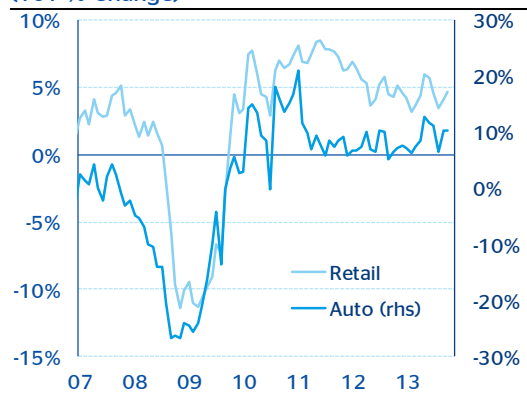
Source: Conference Board and BBVA Research

**Graph 4**  
ISM Indices  
(SA, 50+ = Expansion)



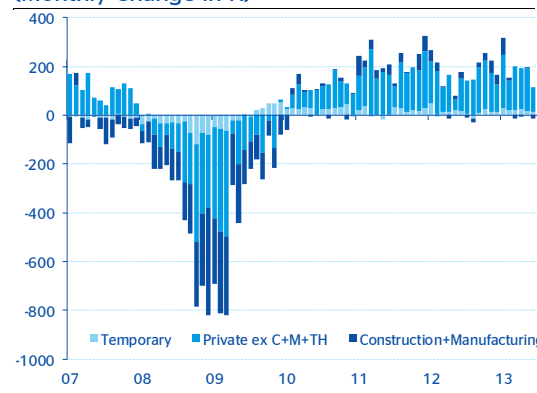
Source: ISM and BBVA Research

**Graph 5**  
Retail and Auto Sales  
(YoY % Change)



Source: US Census Bureau and BBVA Research

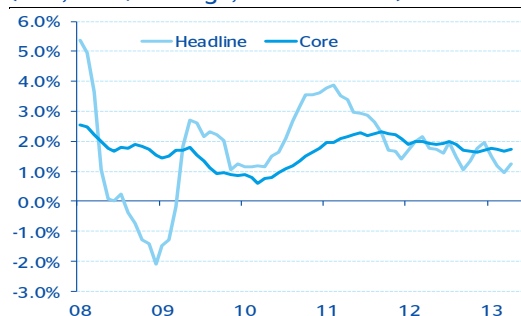
**Graph 6**  
Private Nonfarm Payrolls  
(Monthly Change in K)



Source: BLS and BBVA Research

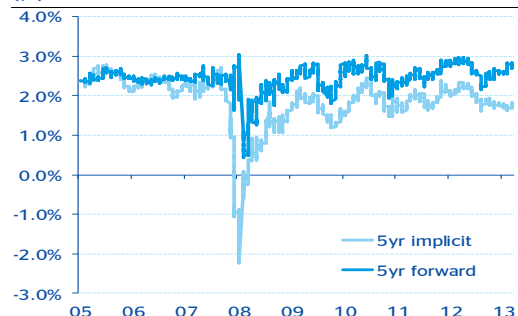
### Economic Indicators

Graph 7  
Consumer Price Index  
(NSA, YoY % Change, 1982-84=100)



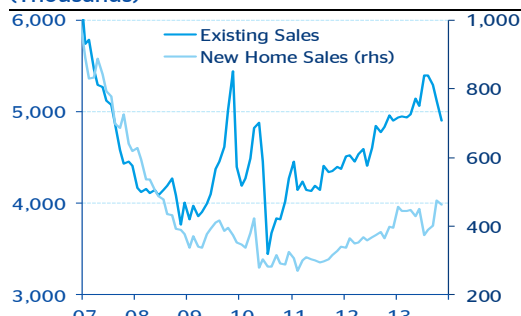
Source: BLS and BBVA Research

Graph 8  
Inflation Expectations  
(%)



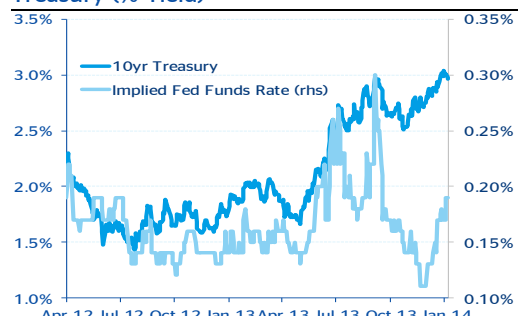
Source: Federal Reserve Board and BBVA Research

Graph 9  
New and Existing Home Sales  
(Thousands)



Source: US Census Bureau, NAR, and BBVA Research

Graph 10  
12-Month Implied Fed Funds Rate & 10-Yr Treasury (% Yield)



Source: Federal Reserve Board and BBVA Research

Table 1  
Forecasts (BOLD=FORECASTS)

	4Q12	1Q13	2Q13	3Q13	2011	2012	<b>2013</b>	<b>2014</b>	<b>2015</b>	<b>2016</b>	<b>2017</b>
Real GDP (% SAAR)	0.1	1.1	2.5	4.1	1.8	2.8	<b>1.8</b>	<b>2.5</b>	<b>2.5</b>	<b>2.8</b>	<b>2.8</b>
Real GDP (Contribution, pp)											
PCE	1.1	1.5	1.2	1.4	1.7	1.5	<b>1.3</b>	<b>1.1</b>	<b>1.2</b>	<b>1.2</b>	<b>1.1</b>
Gross Investment	-0.4	0.7	1.4	2.6	0.7	1.4	<b>0.8</b>	<b>1.1</b>	<b>0.9</b>	<b>1.1</b>	<b>0.9</b>
Non Residential	1.1	-0.6	0.6	0.6	0.8	0.9	<b>0.3</b>	<b>0.7</b>	<b>0.9</b>	<b>0.9</b>	<b>0.8</b>
Residential	0.5	0.3	0.4	0.3	0.0	0.3	<b>0.4</b>	<b>0.3</b>	<b>0.3</b>	<b>0.3</b>	<b>0.3</b>
Exports	0.2	-0.2	1.0	0.5	0.9	0.5	<b>0.3</b>	<b>0.7</b>	<b>0.9</b>	<b>0.8</b>	<b>0.9</b>
Imports	0.5	-0.1	-1.1	-0.4	-0.8	-0.4	<b>-0.2</b>	<b>-0.5</b>	<b>-0.5</b>	<b>-0.3</b>	<b>-0.4</b>
Government	-1.3	-0.8	-0.1	0.1	-0.7	-0.2	<b>-0.4</b>	<b>0.0</b>	<b>0.0</b>	<b>0.0</b>	<b>0.0</b>
Unemployment Rate (% average)	7.8	7.7	7.6	7.3	8.9	8.1	<b>7.4</b>	<b>6.8</b>	<b>6.2</b>	<b>5.7</b>	<b>5.2</b>
Average Monthly Nonfarm Payroll (K)	209	207	182	167	175	183	<b>186</b>	<b>201</b>	<b>226</b>	<b>243</b>	<b>243</b>
CPI (YoY %)	1.9	1.7	1.4	1.6	3.1	2.1	<b>1.5</b>	<b>2.3</b>	<b>2.4</b>	<b>2.4</b>	<b>2.5</b>
Core CPI (YoY %)	1.9	1.9	1.7	1.7	1.7	2.1	<b>1.8</b>	<b>2.0</b>	<b>2.3</b>	<b>2.4</b>	<b>2.5</b>
Fiscal Balance (% GDP)	-	-	-	-	-8.7	-6.8	<b>-4.0</b>	<b>-3.4</b>	<b>-2.2</b>	<b>-2.4</b>	<b>-2.6</b>
Current Account (bop, % GDP)	-2.5	-2.5	-2.3	-2.3	-3.0	-3.0	<b>-2.5</b>	<b>-3.3</b>	<b>-3.2</b>	<b>-2.9</b>	<b>-2.3</b>
Fed Target Rate (% eop)	0.25	0.25	0.25	0.25	0.25	0.25	0.25	<b>0.25</b>	<b>0.50</b>	<b>1.50</b>	<b>2.50</b>
S&P Case-Shiller Index (YoY %)	7.30	9.94	9.88	11.19	-4.34	2.81	<b>11.96</b>	<b>9.25</b>	<b>6.86</b>	<b>5.78</b>	<b>4.91</b>
10-Yr Treasury (% Yield, eop)	1.72	1.96	2.30	2.81	1.98	1.72	2.90	<b>3.37</b>	<b>3.64</b>	<b>4.05</b>	<b>4.24</b>
U.S. Dollar / Euro (eop)	1.31	1.30	1.32	1.34	1.32	1.31	1.37	<b>1.30</b>	<b>1.38</b>	<b>1.36</b>	<b>1.36</b>
Brent Oil Prices (dpb, average)	110.3	112.6	102.7	110.3	111.3	111.7	108.7	<b>112.9</b>	<b>117.2</b>	<b>120.2</b>	<b>124.2</b>

Source: BBVA Research

**DISCLAIMER**

This document was prepared by Banco Bilbao Vizcaya Argentaria's (BBVA) BBVA Research U.S. on behalf of itself and its affiliated companies (each BBVA Group Company) for distribution in the United States and the rest of the world and is provided for information purposes only. Within the US, BBVA operates primarily through its subsidiary Compass Bank. The information, opinions, estimates and forecasts contained herein refer to the specific date and are subject to changes without notice due to market fluctuations. The information, opinions, estimates and forecasts contained in this document have been gathered or obtained from public sources, believed to be correct by the Company concerning their accuracy, completeness, and/or correctness. This document is not an offer to sell or a solicitation to acquire or dispose of an interest in securities.