

Economic Outlook

U.S. Monthly Update

February 20, 2014

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Meeting Details

Topic: U.S. Monthly Economic Outlook Date: Thursday, February 20, 2014 Time: 10:00 am, Central Standard Time (Chicago, GMT-06:00) Meeting Number / Access Code: 718 465 738 Meeting Password: bbva

To join the online meeting:

https://bbvacompass.webex.com/bbvacompass/j.php?MTID=m947db6b5 d38531bc1cec760ca3dce55f

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:

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Baseline Scenario

GDP More surprises ahead?	 As expected, upside risks materialize Less fiscal drag after budget deal Lower policy uncertainty could boost private investment and hiring GDP growth revised from 2.3% to 2.5% for 2014
Inflation Cautious, but not worried	 Although low inflation has persisted for longer than expected, deflationary risks remain low Upside risks in check as economic slack continues
Fed Policy firming vs. thresholds	 Pace of tapering data dependent FOMC debates best strategy for forward guidance Fed funds scenario unchanged; rate hike no earlier than 2015
Interest Rates Trending upward	 Conditional forecasts suggest an orderly adjustment of long-term yields, reaching 4.0% in 2016-2017 An early exit environment would imply a further 100bp adjustment
Risks Tilted to the upside	 Upside: productivity shock, energy/high-tech, low policy drag Downside: debt ceiling, QE3 disorderly exit, financial instability, demographics Global: European/EM crisis, commodity prices, geopolitical

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Baseline Scenario

Upward bias to 2014 growth

	2011	2012	2013	2014	2015	2016	2017	2018
GDP new	1.8	2.8	1.9	2.5	2.5	2.8	2.8	2.9
old	1.8	2.8	1.6	2.3	2.5	2.8	2.8	
CPI new	3.1	2.1	1.5	2.3	2.4	2.4	2.5	2.5
old	3.1	2.1	1.7	2.2	2.4	2.4	2.6	
Core new	1.7	2.1	1.8	2.0	2.3	2.4	2.5	2.5
old	1.7	2.1	1.8	2.0	2.1	2.3	2.6	
Fed new	0.25	0.25	0.25	0.25	0.50	1.50	2.50	3.25
[eop] old	0.25	0.25	0.25	0.25	0.50	1.50	2.50	



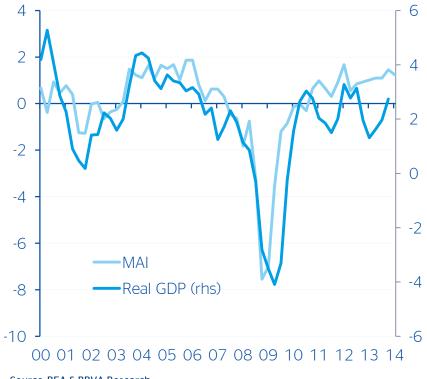
Short-term data suggest a slight slowdown in 1Q14, but overall growth for 2014 expected to outpace most of the recovery thus far

Real GDP & Monthly Activity Index

RESEARCH

4Q % Change

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PCE & Nonresidential Investment

YoY SAAR % Change



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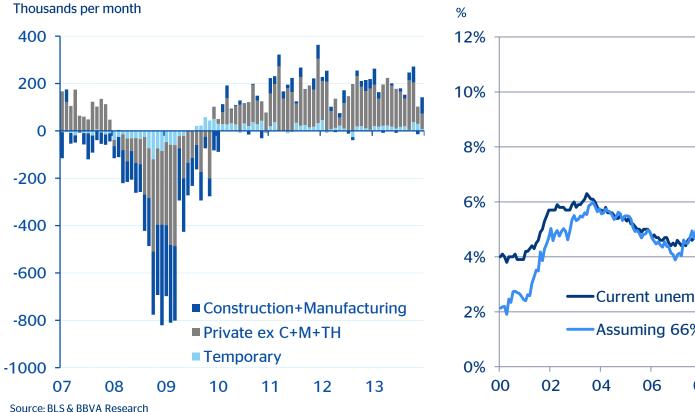
RESEARCH

Labor Markets

Recent trends lack clarity in assessing the true strength of the labor market, even with a drop to 6.6% unemployment

Private Nonfarm Payrolls

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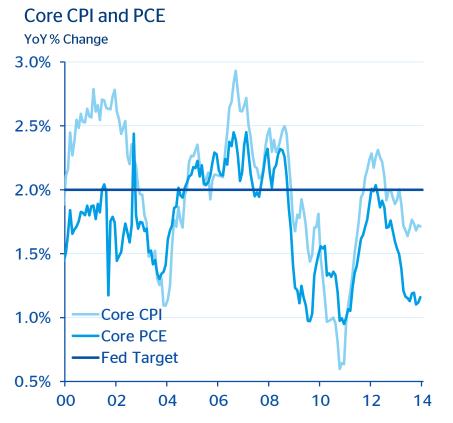
Unemployment Rate





Inflation

Persistently low inflation reflects elevated slack in the labor market and downward price pressures on imported goods





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Monetary Policy

Expected End QE3

The Fed continues to wind-down QE3 with the first unanimous vote since 2011

	Latest	What do we expect?	Policy pause until
Fed	 FOMC Statement Jan. 28th-29th Pace of LSAP reduced to \$65bn Forward guidance and thresholds kept unchanged FOMC repeated its commitment to the course of tapering conditional on labor market and inflation outlook stating: "the Committee will likely reduce the pace of asset purchases in further measured steps at future meetings" 	 Measured steps of \$10bn reduction, evenly split between Treasuries and MBS Tapering remains data driven and conditional on current economic trends. FOMC will continue to discuss alternatives to narrow the gap between the timing of policy firming and the unemployment rate threshold. 	September 2015
Expected Timeline for Exit Strategy	< <u>4Q14</u>	<u>3Q15</u> <u>1H</u>	→ 16

First FFR Hike

Policy Normalization



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Monetary Policy

Shift to more centrist FOMC in 2014

- Rotating regional Bank Presidents were in place to cast their policy vote in January
- Yellen sworn in as Fed Chair on February 3rd, committed to staying the Fed's course
- Vice-chair nominee Fischer and two governor nominees Brainard and Powell await Congressional confirmation with one vacant governor seat still to fill

FOMC 2014 Dove - Hawk Scale	Hawk	Hawkish	Centrist	Dovish	Dove
Yellen (Chair)				{ }	
Fischer (per Congress confirmation, Vice-Chair)					
Tarullo (Governor)				1 1	
Brainard (per Congress confirmation, Governor)				1	
Powell (per Congress confirmation, Governor)					
Stein (Governor)					
Dudley (Permanent, New-York FRB)				· · · · · ·	
Kocherlakota (Rotating, Minneapolis FRB)				} }	
Pianalto (Rotating, Cleveland FRB)				}	
Plosser (Rotating, Philadelphia FRB)					
Fisher (Rotating, Dallas FRB)		} 			

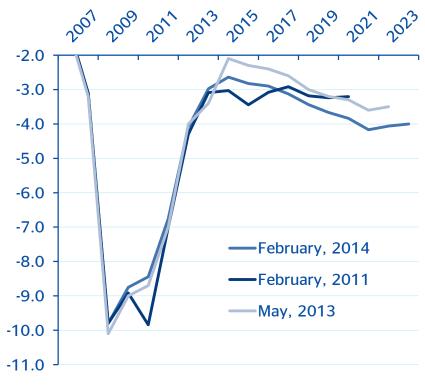


Fiscal Policy

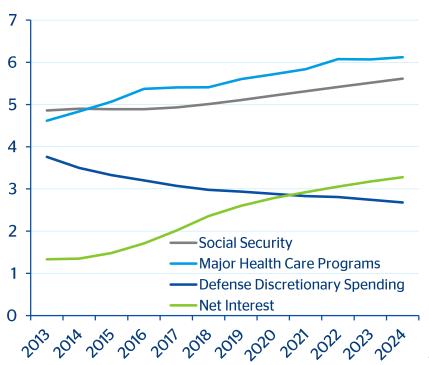
Improved short-term budget outlook, but long-term uncertainty remains

CBO Budget Balance Projections

% of GDP



Projected Government Spending % of GDP



Source: CBO & BBVA Research



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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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