

U.S.

Weekly Watch

April 11, 2011

Economic Analysis

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Highlights

The Fed sees inflation risks tilted to the upside, but still under control

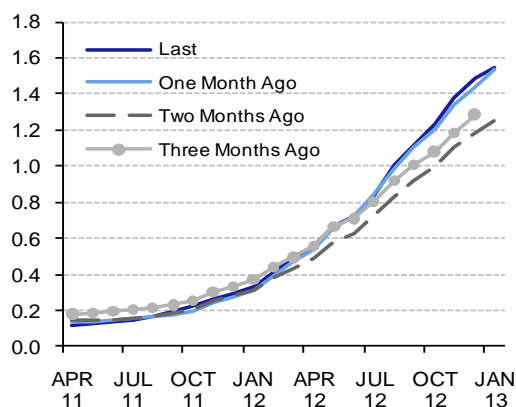
The release of the FOMC minutes reveals that the Fed will not taper its purchases of treasury securities towards the end of its current large-scale asset purchase program. The central bank believes the depth and liquidity of the treasury market precludes the necessity of tapering. FOMC members regard recent commodity price increases as largely transitory. Participants view measures of underlying inflation as subdued, but “bottoming out” compared to historical data. Staff economists reported that market measures and survey indicators of long-term inflation expectations remained stable. However, in general, FOMC members are biased towards upside risks for their inflation forecasts, although their forecasts are still within their comfort zone. A few FOMC members were prompted by this discussion to note that a numerical inflation target would help solidify these expectations. On the other hand, the outlook for economic growth is more balanced. This is the result of a number of competing domestic and international factors. For example, FOMC members still view downside risks from geopolitical strife, fiscal and banking consolidation in Europe, a depressed housing market, and US fiscal reform at the state and Federal level. The text of the minutes suggest more heightened discussion of the accommodation stance, with some members viewing current data as warranting less accommodation, while a few other members’ view of the data supports accommodation beyond 2011. In sum, the minutes confirm our baseline scenario that QE2 will be implemented as planned and that there will be no rate hike throughout the year.

Consumer credit increased in February

The Federal Reserve announced that consumer credit increased 3.75% MoM (\$7.62bn MoM change) at an annual rate in February 2011. The release shows that while non-revolving consumer credit, such as auto and student loans, jumped 7.75%, revolving consumer credit (i.e. credit cards) dropped 4% at an annual rate. The main drivers of this increase in non-revolving credit were auto and student loans. The increase in student loans is reflection of the fact that many people are headed to school as a result of the downturn.

Graph 1

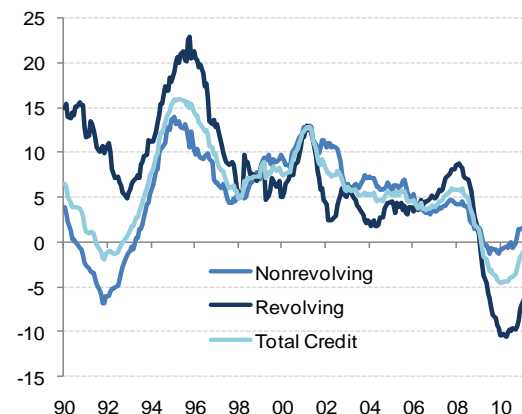
Fed Funds Expectations (Futures Contract End, %)



Source: Bloomberg and BBVA Research

Graph 2

Consumer Credit (YoY % change)



Source: Federal Reserve

Week Ahead

Trade Balance (February, Tuesday 08:30 ET)

Forecast: -\$45.0bn	Consensus: -\$44.0bn	Previous: -\$46.3bn
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The trade balance is expected to shrink slightly in February. We expect that a weak dollar and more robust performance in exports will help reduce the U.S. trade deficit. However, import prices have increased 1.4% MoM on average in the last five months. Therefore, an increase in the value of imports and higher energy prices will limit improvement in the trade balance.

Retail Sales, excl. auto (March, Wednesday 08:30 ET)

Forecast: 0.5%, 0.7%	Consensus: 0.5%, 0.7%	Previous: 1.0%, 0.7%
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Current macroeconomic indicators such as high consumer confidence and recent improvements in labor markets support robust personal spending and retail sales. Although recent increases in oil prices are expected to negatively affect auto sales, high consumer prices will also push up retail sales in nominal terms.

Consumer Price Index, core (March, Friday 08:30 ET)

Forecast: 0.5%, 0.2%	Consensus: 0.5%, 0.2%	Previous: 0.5%, 0.2%
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In February, consumer prices surged mainly due to increases in oil and food prices. The price index for energy commodities jumped 19.3% YoY while the price index for energy services increased only by 0.2%. Monthly increases in headline consumer prices were the largest since June 2009. Of the core price indices, shelter prices are also no longer a drag on core inflation. They have increased by 0.1% MoM on average in the previous five months. We believe that recent increases in oil prices are transitory, therefore posing no long-term threat to price stability, at least for now. We expect that increases in oil prices will continue to push headline inflation higher. However, the pass-through effect from higher energy prices to core prices will remain limited.

Industrial Production Index (March, Friday 09:15 ET)

Forecast: 0.7%	Consensus: 0.6%	Previous: 0.0%
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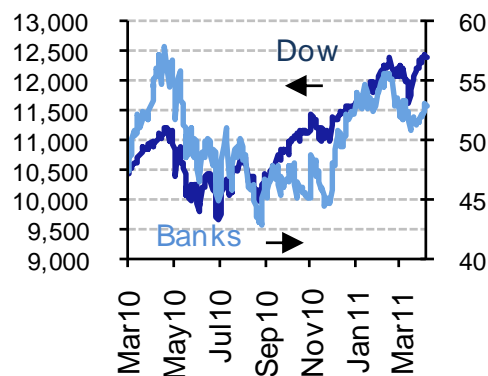
In the first two months of 2011, industrial production (IP) has evolved slower than expected. Although regional manufacturing, ISM manufacturing and ISM services indices point to strong economic activity, the Federal Reserve announced that IP increased by 0.1% MoM on average in the previous two months, compared to 0.6% on average in 2010. We expect that IP will increase around 0.7% MoM, indicating robust economic activity in March and compatible with other macroeconomic indicators.

Market Impact

This week, the market's focus will be on the release of consumer and producer price indices. Both markets and the Fed expect limited pass-through from oil and food prices into underlying inflation. If consumer prices, particularly core prices, increase more than the market expectation, it would imply a higher pass-through effect and therefore would increase inflation expectations.

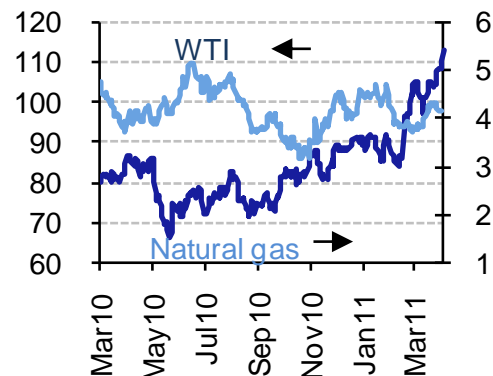
Financial Markets

Graph 3
Stocks (Index, KBW)



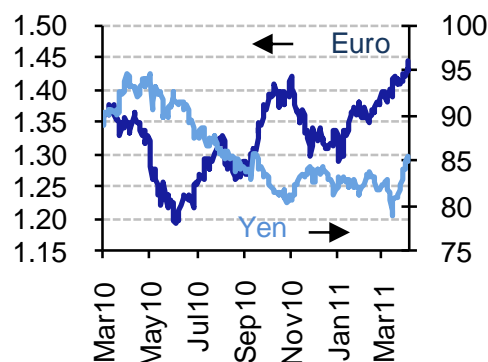
Source: Bloomberg & BBVA Research

Graph 4
Commodities (Dpb & DpMMBtu)



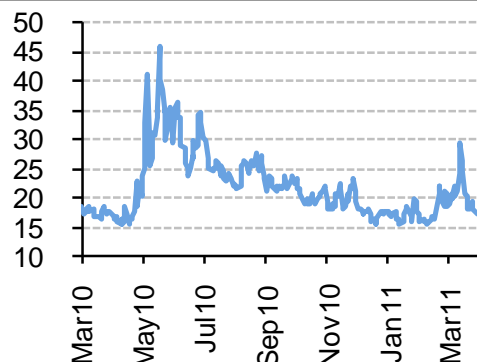
Source: Bloomberg & BBVA Research

Graph 5
Currencies (Dpe & Ypd)



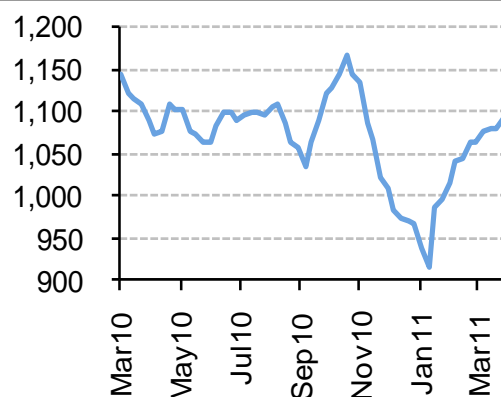
Source: Bloomberg & BBVA Research

Graph 6
Volatility (Vix, Index)



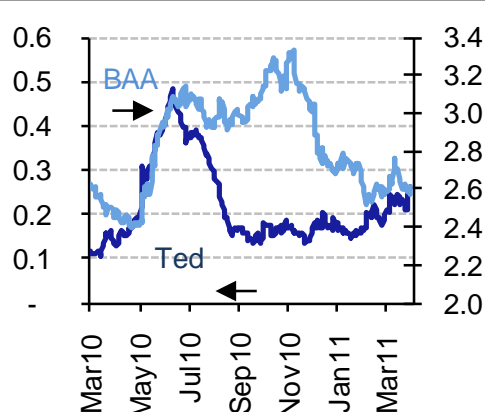
Source: Bloomberg & BBVA Research

Graph 7
Commercial Paper Issuance (US\$Bn)



Source: Bloomberg & BBVA Research

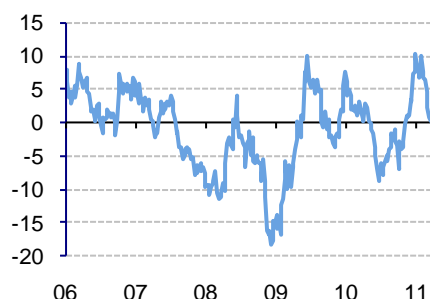
Graph 8
TED & BAA Spreads (%)



Source: Bloomberg & BBVA Research

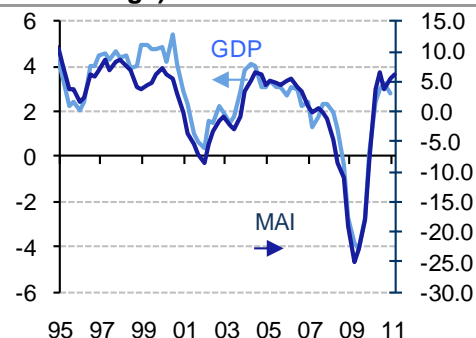
Economic Trends

Graph 9
**BBVA US Weekly Activity Index
(3 month % change)**



Source: BBVA Research

Graph 10
**BBVA US Monthly Activity Index & Real
Gross Domestic Product
(4Q % change)**



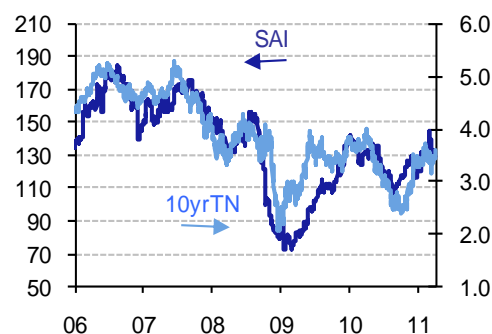
Source: BBVA Research & BEA

Graph 11
**BBVA US Surprise Inflation Index
(Index 2009=100)**



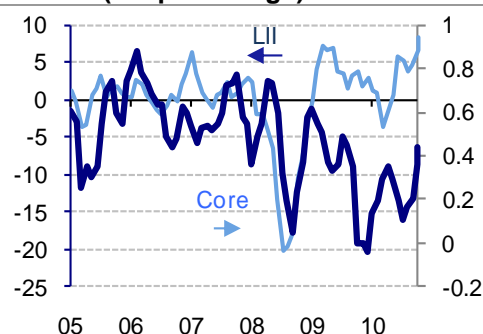
Source: BBVA Research

Graph 12
**BBVA US Surprise Activity Index & 10-yr
Treasury (Index 2009=100 & %)**



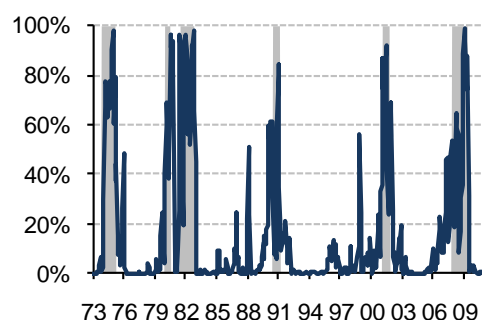
Source: Bloomberg & BBVA Research

Graph 13
**BBVA US Leading Inflation Index & Core
Inflation (QoQ % change)**



Source: BLS & BBVA Research

Graph 14
**BBVA US Recession Probability Model
(Recession episodes in shaded areas, %)**



Source: BBVA Research

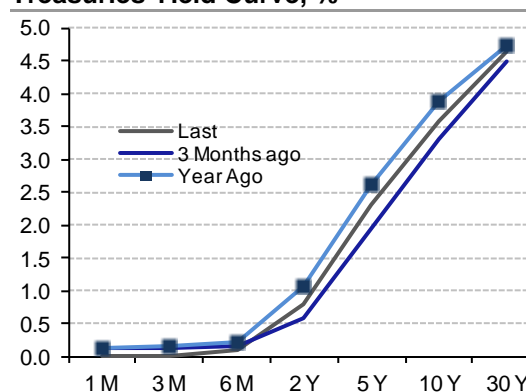
Yield Curve and Interest Rates

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)	13.73	13.73	13.73	12.97
New Auto (36-months)	4.26	4.28	4.80	6.50
Heloc Loan 30K	5.47	5.48	5.48	5.66
30-year Fixed Mortgage *	4.87	4.86	4.88	5.21
Money Market	0.62	0.63	0.61	0.79
2-year CD	1.25	1.25	1.28	1.63
5-year CD	2.07	2.07	2.06	2.58

* Freddie Mac National Mortgage Homeowner Commitment 30 Year US
Source: Bloomberg and BBVA Research

Graph 15
Treasuries Yield Curve, %



Source: Bloomberg

Quote of the Week

Federal Reserve Bank of Atlanta President Dennis P. Lockhart
April 8, 2011
Knoxville Economics Forum
Knoxville, Tenn.

"...my expectation is that commodity price increases that are now translating into accelerating headline inflation will be transitory."

Economic Calendar

Date	Event	Period	Forecast	Survey	Previous
12-Apr	NFIB Small Business Optimism	MAR	94.4	94.9	94.5
12-Apr	Import Price Index (MoM)	MAR	2.0%	2.1%	1.4%
12-Apr	Import Price Index (YoY)	MAR	8.60%	9.10%	6.90%
12-Apr	Trade Balance	FEB	-\$45.0B	-\$44.0B	-\$46.3B
12-Apr	Monthly Budget Statement	MAR	-\$189.0B	-\$189.0B	- -
13-Apr	Advance Retail Sales	MAR	0.5%	0.5%	1.0%
13-Apr	Retail Sales Less Autos	MAR	0.7%	0.7%	0.7%
13-Apr	Business Inventories	FEB	0.7%	0.8%	0.9%
13-Apr	Fed's Beige Book	--	--	--	--
14-Apr	Initial Jobless Claims	9-Apr	378K	380K	382K
14-Apr	Continuing Claims	2-Apr	3705K	3710K	3723K
14-Apr	Producer Price Index (MoM)	MAR	1.3%	1.1%	1.6%
14-Apr	PPI Ex Food & Energy (MoM)	MAR	0.3%	0.2%	0.2%
14-Apr	Producer Price Index (YoY)	MAR	6.4%	6.2%	5.6%
14-Apr	PPI Ex Food & Energy (YoY)	MAR	2.0%	1.9%	1.8%
15-Apr	Consumer Price Index (MoM)	MAR	0.5%	0.5%	0.5%
15-Apr	CPI Ex Food & Energy (MoM)	MAR	0.2%	0.2%	0.2%
15-Apr	Consumer Price Index (YoY)	MAR	2.7%	2.6%	2.1%
15-Apr	CPI Ex Food & Energy (YoY)	MAR	1.30%	1.20%	1.10%
15-Apr	Empire Manufacturing	APR	17.0	16.9	17.5
15-Apr	Industrial Production	MAR	0.70%	0.60%	0.00%
15-Apr	Capacity Utilization	MAR	77.3%	77.4%	77.0%
15-Apr	U. of Michigan Confidence	APR P	66.0	69.0	67.5

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