

Weekly Watch

U.S.

Highlights

8 August 2011
Economic Analysis

U.S.

Boyd Stacey
boyd.stacey@bbvacompass.com

Kim Fraser
kim.fraser@bbvacompass.com

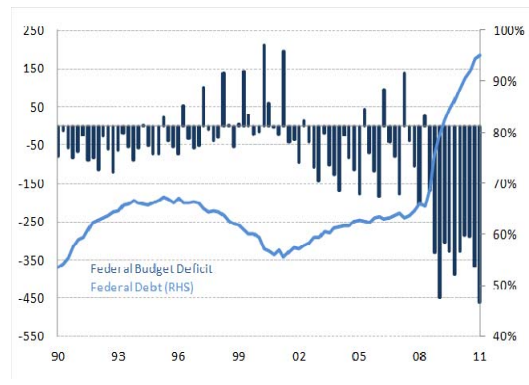
Debt ceiling resolution calms markets, only first step towards austerity

This week Congress passed the Budget Control Act, increasing the United States' borrowing authority after months of political histrionics. The proposed legislation involves \$917bn in deficit reduction between 2012 and 2021, with a committee plan for an additional \$1.2tr in scheduled cuts if no committee consensus is reached before 2013. The first substantial cuts will occur in 2013 and will involve \$350bn in defense spending cuts. Acceleration of nondefense related spending is back-loaded, giving Democrats more time to address the current tax code inefficiencies, which could offset cuts to entitlements and health care. In addition, a hard \$1.2tr discretionary cap and a mandated \$1.5tr in deficit reduction over the next ten years will force committee negotiations to entertain compromises. The rigidity of the mandated cuts and oversight powers now enjoyed by the White House should give markets transparency to markets, in regards to fiscal sustainability. However, the proposed deal is not the ultimate compromise to eradicate debt concerns, and further fiscal reform is required. Although the debt ceiling resolution reduces the chance of a US ratings downgrade, more consolidation is necessary in order to avert any future downgrade. Despite the outlook for another contentious round of political histrionics, we expect that necessary measures will pass.

Employment situation rebounds, better-than-expected nonfarm payrolls

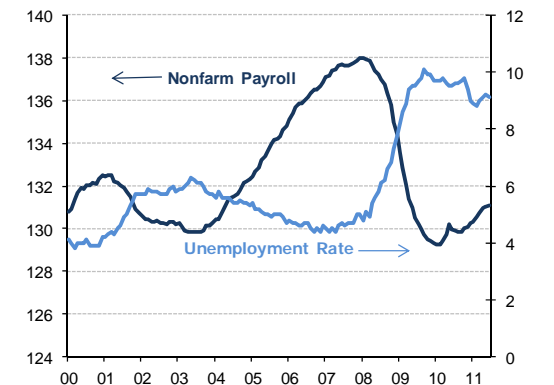
The Employment Situation released today indicated that nonfarm payrolls jumped 117k in July from a revised 46k last month, beating consensus estimates of 75k. The positive report suggests a better employment outlook than the disappointing report in June. Total private payrolls drove the job increase in July, coming in at 154k, primarily in the service-providing sector. On the downside, government employment declined for the tenth straight month, shrinking by 37k jobs. The unemployment rate fell back to 9.1% in July after increasing to 9.2% last month. The MoM decline, with no change to the number of unemployed (13.2M), suggests the decline is a function of a decreasing labor force participation, which declined to 63.9%. In addition, average hourly earnings increased 0.4% MoM following no change in June. The steady declines in initial jobless claims throughout the past few weeks could be an indication of job market growth for 2H11. Furthermore, the better-than-expected employment data for July could reduce uncertainties regarding the future outlook for the U.S. economy.

Chart 1
Federal Budget Deficit (\$bn) and Debt to GDP Ratio (%)



Source: CBO & Treasury Department

Chart 2
Nonfarm Payroll (k) and Unemployment Rate (%)



Source: BLS

Week Ahead

FOMC Rate Decision (August, Tuesday 14:15 ET)

Forecast: 0.0%- 0.25%	Consensus: 0.0%-0.25%	Previous: 0.0%- 0.25%
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1Q11 GDP was revised down to 0.4% QoQ annualized compared to previous estimates between 1.8% and 1.9%. More importantly, the last quarter's revision and this month's advanced estimates are inconsistent with Fed expectations of 2.5%-3.0% annual growth. However, the positive July employment report could offset some of the negative expectations. Furthermore, the current consumer price growth (PCE) of 1.3% YoY is within the implicit fed range, and the trend is not suggestive of deflation. Thus, we expect this month's meeting to focus on future policy actions and the prospects of 2H11 job growth, with no change to the Fed Funds rate.

International Trade Balance (June, Thursday 8:30 ET)

Forecast: -\$46.9bn	Consensus: -\$48.0bn	Previous: -\$50.2bn
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The trade balance is expected to narrow in June, mostly due to a weakened dollar and expanding exports in the service sector. Import prices were down slightly in June and likely deflated the value of imports, while a slower-than-expected recovery of the U.S. economy may have reduced demand for other imported goods. Auto imports have been declining as a result of the Japanese earthquake disruptions, however supply chains are expected to recover in the coming months. Thus, we expect only limited improvements in the overall trade balance.

Retail Sales (July, Friday 8:30 ET)

Forecast: 0.3%	Consensus: 0.5%	Previous: 0.1%
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Crude and refined crude prices accelerated in July possibly giving a nominal boost to retail gasoline sales. However, we expect auto sales growth to decelerate and health services to decline, resulting in a modest MoM retail sales increase. July's leading monthly service surveys reported that health services contracted in July, though it did indicate the food service sector was growing. Furthermore, Autodata reported an auto sales increase in July. Strong auto sales in combination with strong food service sales suggest a positive MoM gain and the possibility an upside bias to the July report.

Business Inventories (June, Friday 10:00 ET)

Forecast: 1.1%	Consensus: 0.6%	Previous: 1.0%
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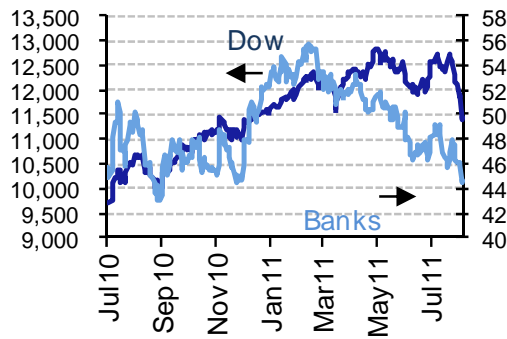
Inventories have been growing steadily and we expect this growth to continue in June as levels approach 3-year highs. Declining consumer confidence and weak demand has contributed to high inventories for manufacturers, retailers, and merchant wholesalers. Durable goods inventories increased in June, mostly due to transportation equipment, and nondurables are likely to continue the 6-month upward trend. Thus, we expect business inventories to remain high in June.

Market Impact

Now that a U.S. default has been avoided, market focus has shifted to uncertainties regarding fiscal reform and weak economic activity. Markets will watch the FOMC announcement closely as future Fed action may ease worries about the economy recovery.

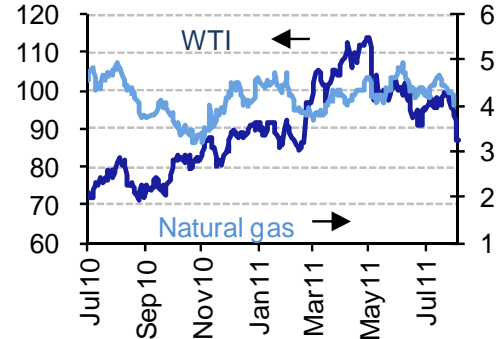
Financial Markets

Graph 3
Stocks (Index, KBW)



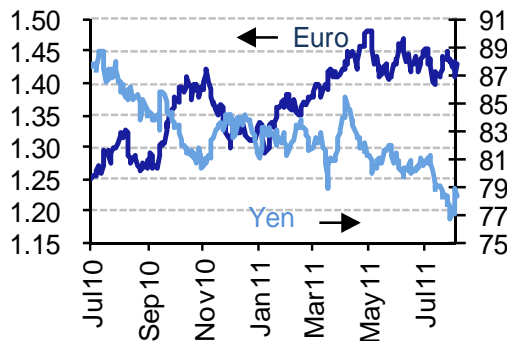
Source: Bloomberg & BBVA Research

Graph 4
Commodities (Dpb & DpMMBtu)



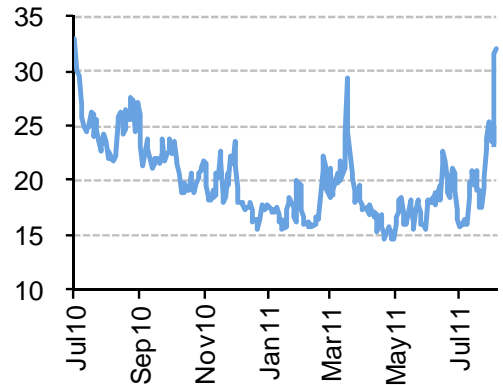
Source: Bloomberg & BBVA Research

Graph 5
Currencies (Dpe & Ypd)



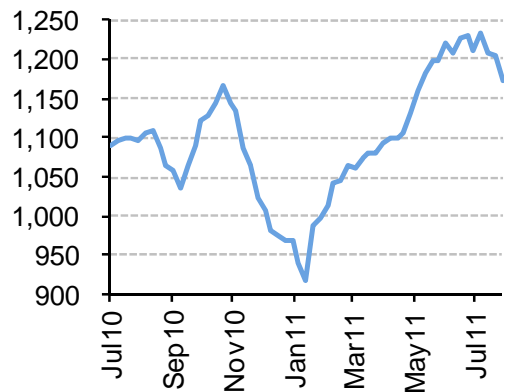
Source: Bloomberg & BBVA Research

Graph 6
Volatility (Vix, Index)



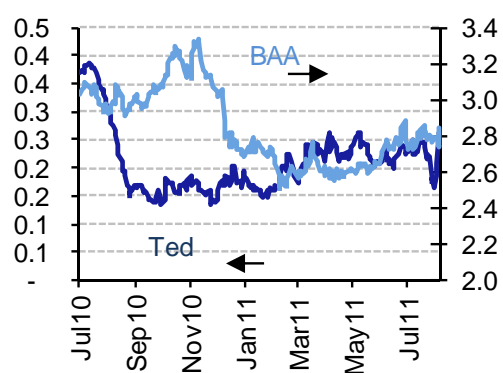
Source: Bloomberg & BBVA Research

Graph 7
Commercial Paper Issuance (US\$Bn)



Source: Bloomberg & BBVA Research

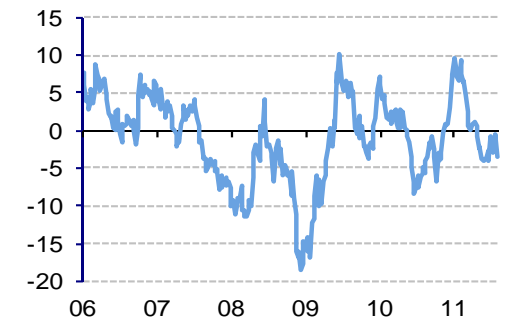
Graph 8
TED & BAA Spreads (%)



Source: Bloomberg & BBVA Research

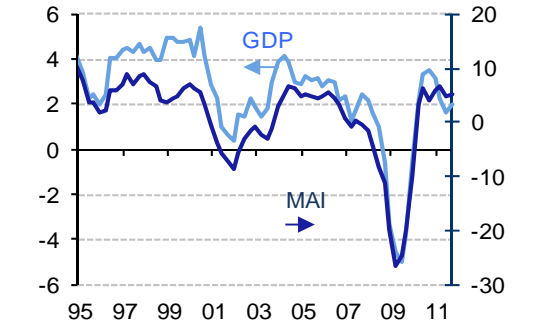
Economic Trends

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)



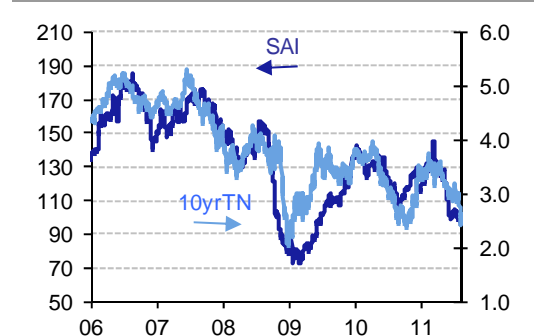
Source: BBVA Research & BEA

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



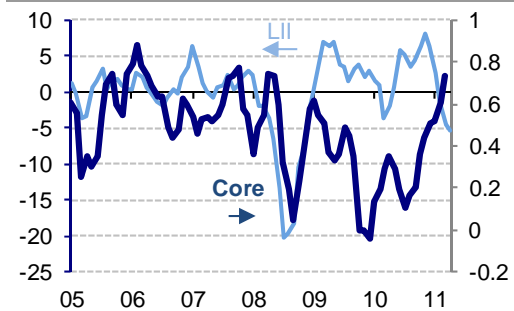
Source: BBVA Research

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



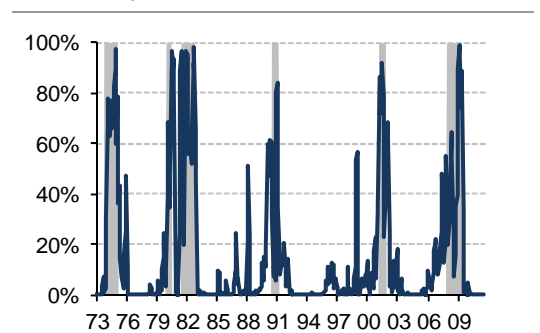
Source: Bloomberg & BBVA Research

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

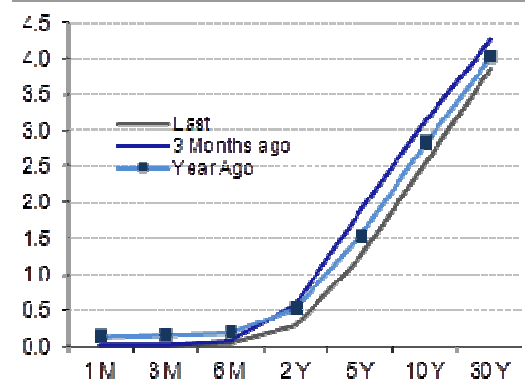
Yield Curve and Interest Rates

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	13.44
New Auto (36-months)	4.30	3.94	3.68	6.16
Heloc Loan 30K	5.54	5.56	5.55	5.59
30-year Fixed Mortgage *	4.39	4.55	4.60	4.49
Money Market	0.58	0.58	0.63	0.74
2-year CD	1.04	1.04	1.06	1.46
5-year CD	2.01	2.01	2.04	2.40

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

Graph 15
Treasury Yield Curve, %



Source: Bloomberg

Quote of the Week

President Barack Obama
Obama Focused on Americans' Employment.
5 August 2011

"My singular focus is the American people; getting the unemployed back on the job, lifting their wages... and helping them recover fully, as families and communities from the worst recession that any of us have ever seen."

Economic Calendar

Date	Event	Period	Forecast	Survey	Previous
9-Aug	Nonfarm Productivity	Q2	-0.1%	-0.8%	1.8%
9-Aug	Unit Labor Costs	Q2	1.0%	2.4%	0.7%
9-Aug	FOMC Rate Decision	AUG	0.25%	0.25%	0.25%
10-Aug	Wholesale Inventories	JUN	1.1%	1.0%	1.8%
10-Aug	Monthly Treasury Budget	JUL	-\$137.4B	-\$135.0B	-\$43.1B
11-Aug	International Trade Balance	JUN	-\$46.9B	-\$48.0B	-\$50.2B
11-Aug	Initial Jobless Claims	5-Aug	395K	401K	400K
11-Aug	Continuing Claims	30-Jul	3725K	3725K	3730K
12-Aug	Advance Retail Sales	JUL	0.3%	0.5%	0.1%
12-Aug	Retail Sales Less Autos	JUL	0.1%	0.2%	0.0%
12-Aug	Consumer Sentiment	AUG	62.0	63.0	63.7
12-Aug	Business Inventories	JUN	1.1%	0.6%	1.0%

Chief Economist for US

Nathaniel Karp
Nathaniel.karp@bbvacompass.com

Ignacio San Martin
Ignacio.SanMartin@bbvacompass.com

Jeffrey Owen Herzog
Jeff.Herzog@bbvacompass.com

Marcial Nava
Marcial.Nava@bbvacompass.com

Kim Fraser
Kim.Fraser@bbvacompass.com

Jason Frederick
Jason.Frederick@bbvacompass.com

Boyd Stacey
Boyd.Stacey@bbvacompass.com

Contact details

BBVA Research
5 Riverway Drive
Houston, Texas 77056

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