

# US Weekly Flash

## Highlights

### • Fed Chairman Addresses Cautions on Economic Outlook

- Ben Bernanke spoke in his semiannual monetary policy report to Congress, reiterating most details that were highlighted in the latest FOMC meeting minutes. The Fed Chairman touched on the recent slowing in economic activity as well as the downside risks to growth, yet no new anecdotal information was revealed. In regards to the labor market, he noted that the slowing in employment growth throughout 2Q12 can only partially be attributed to seasonal adjustment issues and the unusually warm winter weather. The full extent to which these factors have contributed to the loss of labor market momentum will likely be clearer when July's data are released. Despite the recent declines in gas prices that have boosted consumer spending power, uncertain employment and income expectations have kept household confidence low.
- While the usual headwinds to the recovery remain, Bernanke emphasized the significance of the European fiscal and banking crisis and the U.S. fiscal cliff as the two main sources of risk moving forward. European authorities have taken "constructive steps" to improving the fiscal situation in the region, and the U.S. has been working to improve its financial system so as to avoid severe shocks. Still, Bernanke stressed that "European developments that resulted in a significant disruption in global financial markets would inevitably pose significant challenges for our financial system and our economy." Domestically, the impending fiscal cliff remains a significant risk to growth. As in previous statements, Bernanke once again underlined the importance of cooperation in Congress to address these fiscal challenges so as to avoid further deterioration in economic activity. Finally, the Chairman reiterated the Fed's commitment to take further action as appropriate, though he revealed no additional insight on the probability of QE3.

### • Retail Sales Data Disappoint in June, Industrial Production Rebounds

- Retail sales declined for the third consecutive month, down 0.5% in June due in large part to a surprising drop in the auto component. Despite an increase in unit auto sales for the month, the nominal value of motor vehicle sales declined 0.6% following a 0.8% gain in the previous month. Excluding autos, retail sales declined 0.4%. As in the past three months, gasoline sales led the decline, dropping 1.8% in June. While declining gas prices have helped to improve consumers' spending power, the 0.5% drop in real retail sales suggests continued hesitation and uncertainty among consumers.
- In other news, industrial production recovered from previous weakness, increasing 0.4% in June after falling 0.2% in May, with the index reaching its highest level of the recovery. Total output was led by the manufacturing sector, which gained 0.7% to offset the 0.7% decline in the previous month. Given the latest deterioration in other indicators on the sector, growth in manufacturing output is a positive surprise that should ease some worries on slowing activity. While the growth in manufacturing and total output is certainly good news, the data are not necessarily enough to convince FOMC members that we are out of the woods just yet.

### • Upward Pressure on Core Inflation Continues

- The consumer price index was unchanged in June following a 0.3% decline in May. Energy prices continued to decline for the third consecutive month, down 1.4% due in large part to a 2.0% drop in the gasoline index. Food prices helped to offset some of the energy price declines, gaining 0.2% after remaining unchanged in the previous month. Headline inflation remained steady at 1.7% on a YoY basis, in line with our models which suggest an annual rate near 2.0% for 2012.
- However, components other than food and energy continue to exert pressure on core inflation, which increased 0.2% for the fourth consecutive month. In general, inflation data for June are unlikely to have much influence in the next FOMC meeting. Views on the risk of higher inflation will remain divided given the disparity between headline and core figures.

## Week Ahead

### New Home Sales (June, Wednesday 10:00 ET)

Forecast: 373K

Consensus: 372K

Previous: 369K

The housing sector has been showing signs of improvement, but activity involving new homes has been a weak spot in the recovery. New home sales are expected to increase only slightly in June after increasing 7.6% in May and declining in March and April. Other housing data for the month have been relatively positive, with new housing starts reflecting a modest boost in demand. Furthermore, homebuilder confidence in June reached the highest level of the recovery, suggesting that activity continued to gain momentum from previous months.

### Durable Goods Orders, Ex Transportation (June, Thursday 8:30 ET)

Forecast: 0.2%, -0.3%

Consensus: 0.3%, 0.0%

Previous: 1.1%, 0.4%

The usual monthly volatility in durable goods orders has not subsided in recent months, with the indicator jumping in May following two consecutive months of declines. The main driver is often the aircraft orders component, which is likely to grow at a slower pace in June after increasing in the previous month. Slowing in manufacturing activity will likely weigh on the headline figure, with most surveys for June suggesting decelerating new orders. On the bright side, increasing demand for autos may help keep durable goods orders in positive growth territory.

### Initial Jobless Claims (Week of July 21<sup>st</sup>, Thursday 8:30 ET)

Forecast: 380K

Consensus: 380K

Previous: 386K

Jobless claims dropped significantly in early July to the lowest level of the recovery, though most of this was due to the shortened holiday week. The second reading for the month jumped back up to levels more consistent with June's data, suggesting that labor market conditions remain weak. Claims data this time of year are usually volatile given the seasonal adjustments for summer retoolings and shutdowns in the auto sector. It is unlikely that the employment situation has improved dramatically over June given weak consumer prospects regarding current conditions and future income and job availability.

### GDP, Advance Estimate (2Q12, Friday 8:30 ET)

Forecast: 1.9%

Consensus: 1.4%

Previous: 1.9%

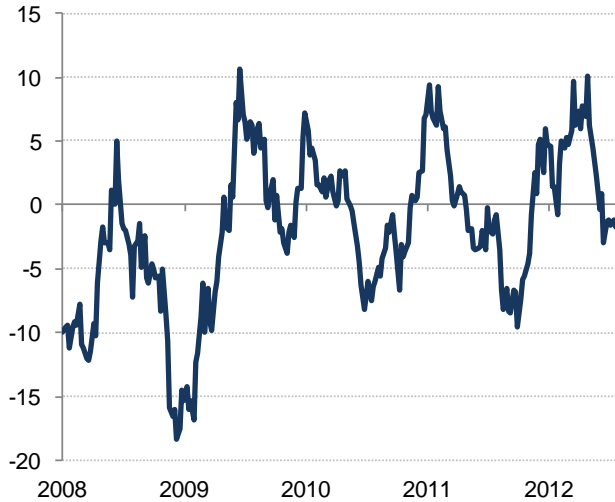
Economic activity has been mixed throughout the second quarter compared to the recovery strength seen earlier in 2012, yet we expect that GDP growth will continue at similar QoQ annualized pace. In regards to the underlying GDP components, improvements in trade and production data will likely offset some of the slowing in inventory and real PCE growth. On average, the trade balance in 2Q12 was slightly better compared to 1Q12 given the improvement in May and the rebound in export growth. Furthermore, industrial production has fared slightly better in the second quarter in terms of average monthly growth. On the downside, inventory growth has been slower compared to the first quarter. Also, real PCE has increased only 0.1% per month on average in 2Q12 thus far compared to more than 0.2% in 1Q12. Still, we expect that the pace of overall GDP growth will not change significantly from the previous quarter.

### Market Impact

Markets will focus mostly on the 2Q12 GDP release, though low expectations will likely result in a downbeat market for the week. Mixed data in recent months have increased uncertainty regarding the strength of the recovery, leaving markets highly sensitive to upcoming housing, manufacturing, and consumer data.

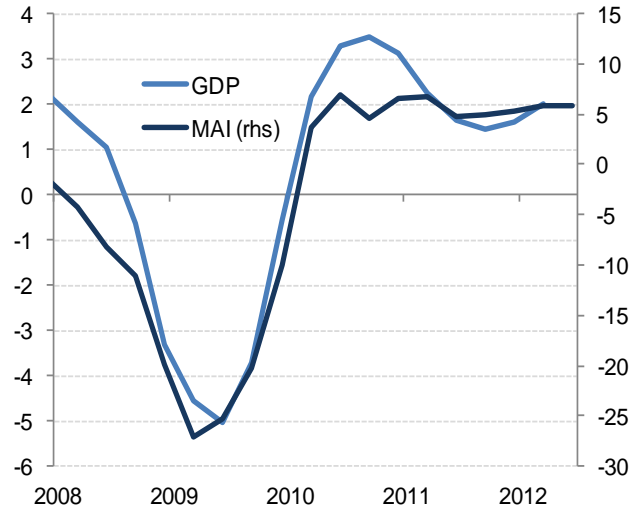
# Economic Trends

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



Source: BBVA Research

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



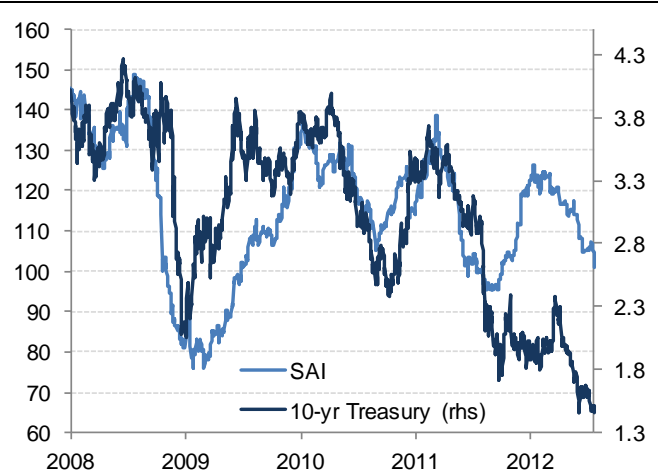
Source: BBVA Research & BEA

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



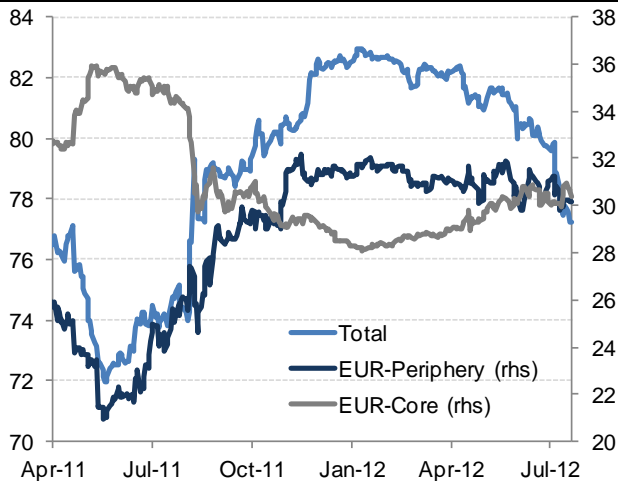
Source: BBVA Research

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



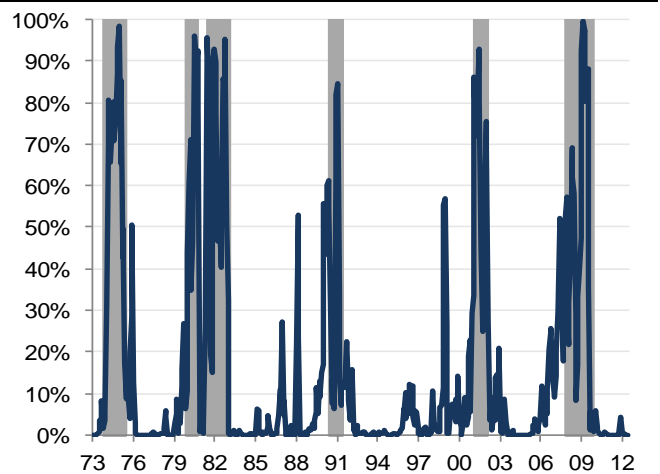
Source: Bloomberg & BBVA Research

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



Source: BBVA Research

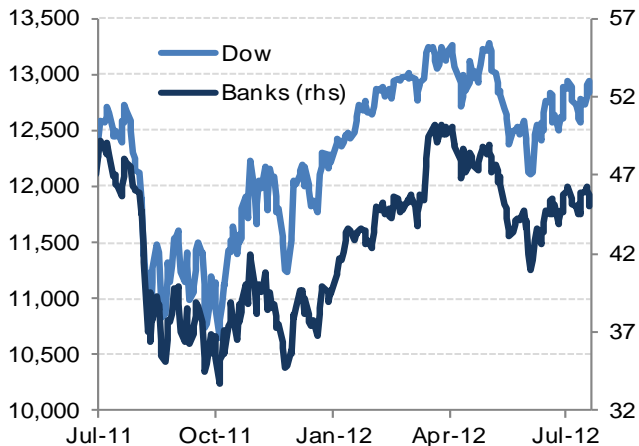
Graph 8  
**BBVA US Recession Probability Model**  
 (Recession episodes in shaded areas, %)



Source: BBVA Research

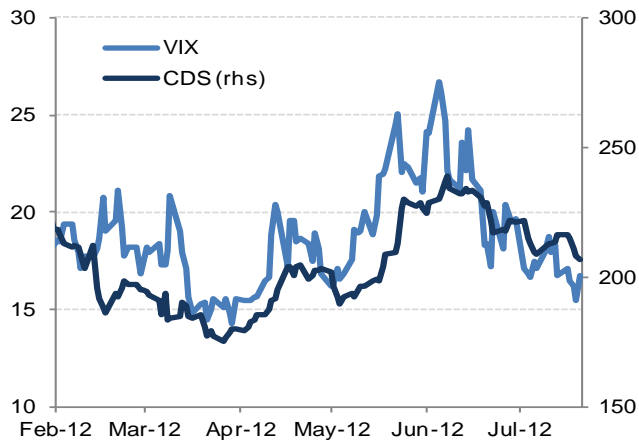
# Financial Markets

Graph 9  
Stocks  
(Index, KBW)



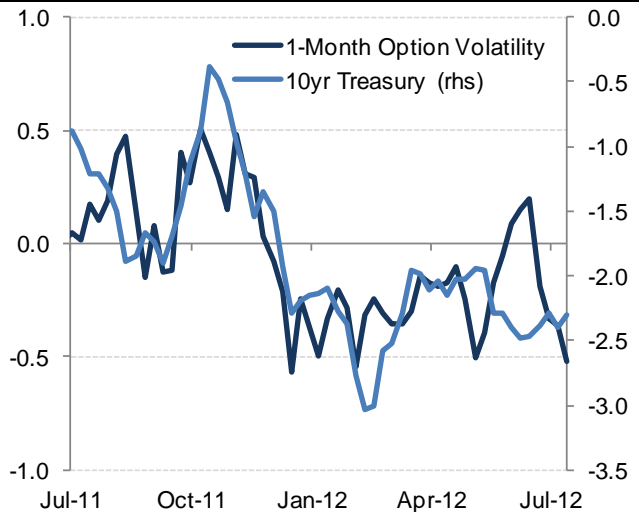
Source: Bloomberg & BBVA Research

Graph 10  
Volatility & High-Volatility CDS  
(Indices)



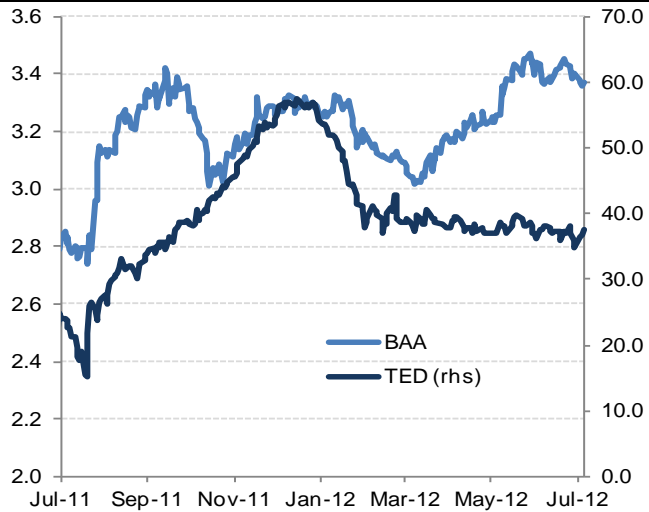
Source: Bloomberg & BBVA Research

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



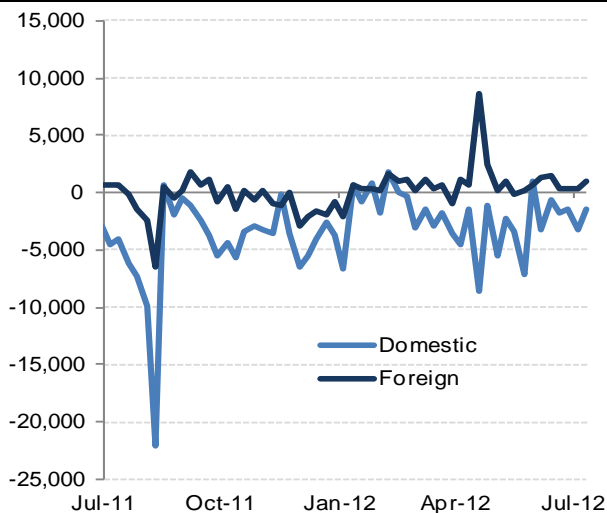
Source: Haver Analytics & BBVA Research

Graph 12  
TED & BAA Spreads  
(%)



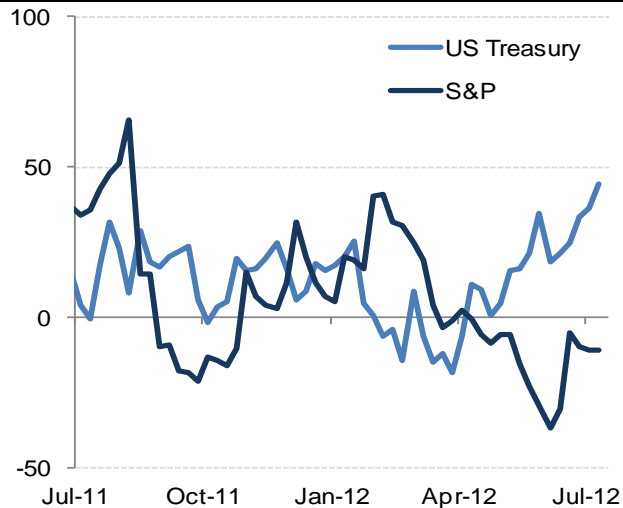
Source: Bloomberg & BBVA Research

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



Source: Haver Analytics & BBVA Research

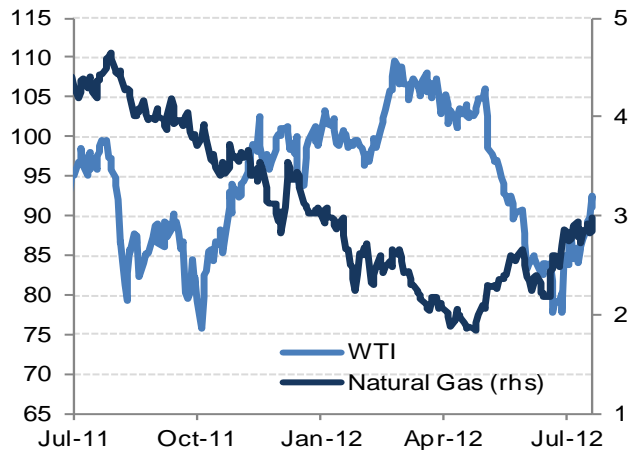
Graph 14  
Total Reportable Short & Long Positions  
(Short-Long, K)



Source: Haver Analytics & BBVA Research

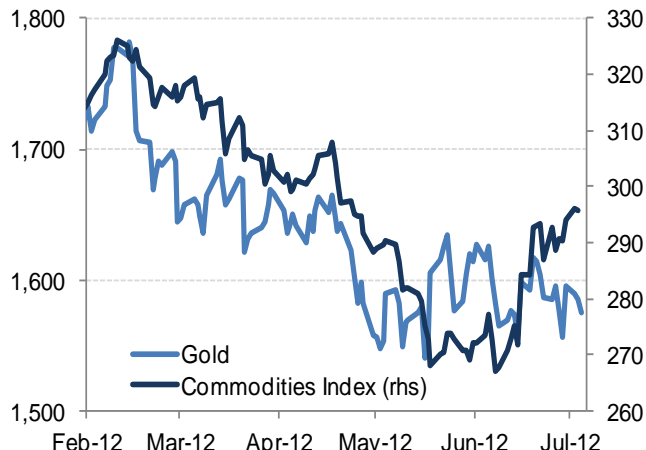
# Financial Markets

Graph 15  
**Commodities**  
 (Dpb & DpMMBtu)



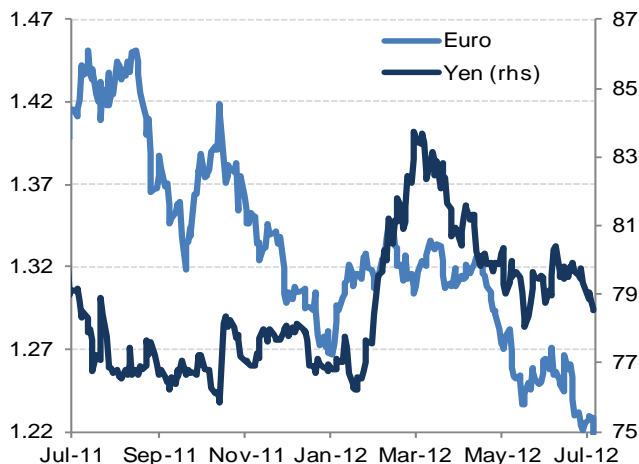
Source: Bloomberg & BBVA Research

Graph 16  
**Gold & Commodities**  
 (US\$ & Index)



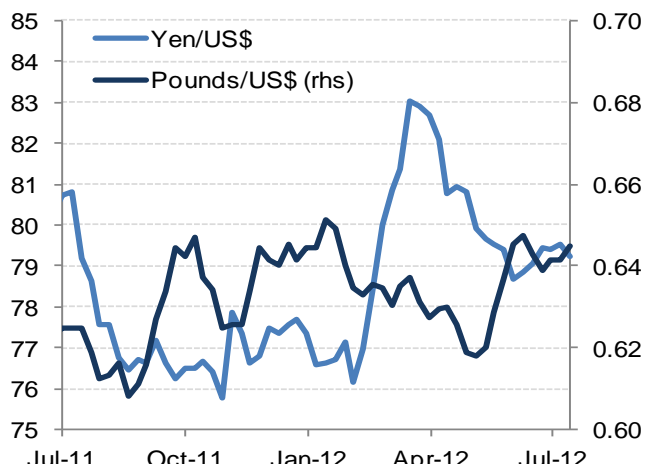
Source: Haver Analytics & BBVA Research

Graph 17  
**Currencies**  
 (Dpe & Ypd)



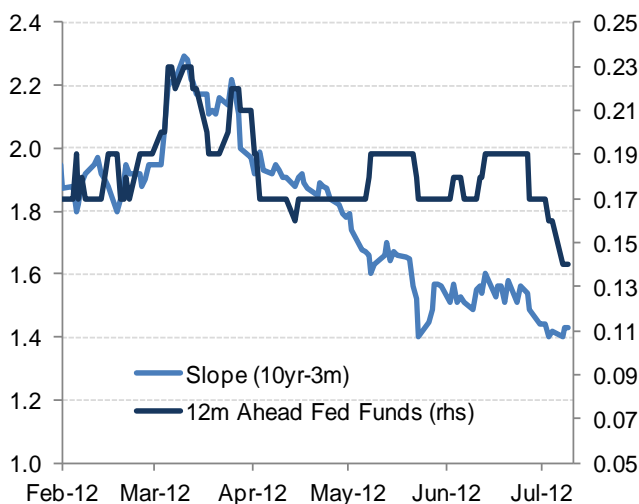
Source: Bloomberg & BBVA Research

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



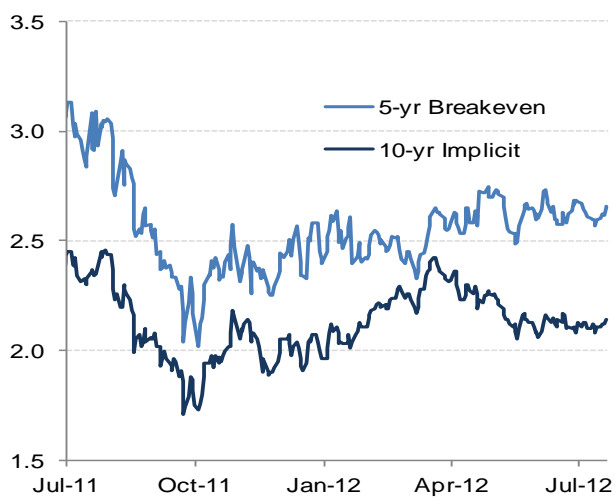
Source: Haver Analytics & BBVA Research

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)	14.10	14.10	14.10	13.73
New Auto (36-months)	3.08	3.11	3.08	3.99
Heloc Loan 30K	5.44	5.47	5.53	5.58
5/1 ARM*	2.69	2.74	2.77	3.27
15-year Fixed Mortgage*	2.83	2.86	2.95	3.66
30-year Fixed Mortgage*	3.53	3.56	3.66	4.52
Money Market	0.50	0.50	0.72	0.60
2-year CD	0.85	0.82	0.90	1.04

\*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	0.13	0.19	0.17	0.06
3M Libor	0.45	0.46	0.47	0.25
6M Libor	0.73	0.73	0.74	0.42
12M Libor	1.06	1.07	1.07	0.75
2yr Sw ap	0.45	0.46	0.55	0.62
5yr Sw ap	0.81	0.85	1.01	1.78
10Yr Sw ap	1.60	1.62	1.81	3.06
30yr Sw ap	2.31	2.33	2.50	3.92
7day CP	0.21	0.21	0.34	0.21
30day CP	0.28	0.24	0.29	0.20
60day CP	0.33	0.23	0.31	0.24
90day CP	0.38	0.24	0.38	0.23

Source: Bloomberg & BBVA Research

## Quote of the Week

Ben Bernanke, Federal Reserve Chairman  
Bernanke Says Fed Can Remove 'Punch Bowl,' Curb Inflation  
18 July 2012

*"It will be a similar pattern to what we've seen in previous episodes where the Fed cut rates, provided support for the recovery, and when the recovery reached a point of takeoff where it could support itself on its own, then the Fed pulled back, took away the punch bowl."*

## Economic Calendar

Date	Event	Period	Forecast	Survey	Previous
23-Jul	Chicago Fed National Activity Index	JUNE	-0.15	--	-0.45
25-Jul	New Home Sales	JUNE	373K	372K	369K
25-Jul	New Home Sales (MoM)	JUNE	1.08%	0.80%	7.60%
26-Jul	Durable Goods Orders	JUNE	0.20%	0.30%	1.10%
26-Jul	Durable Goods Orders Ex Transportation	JUNE	-0.30%	0.00%	0.40%
26-Jul	Initial Jobless Claims	21-Jul	380K	380K	386K
26-Jul	Continuing Claims	14-Jul	3310K	3300K	3314K
26-Jul	Pending Home Sales (MoM)	JUNE	0.20%	0.90%	5.90%
27-Jul	GDP QoQ Annualized	2Q12 A	1.90%	1.40%	1.90%
27-Jul	Personal Consumption	2Q12 A	1.80%	1.40%	2.50%
27-Jul	GDP Price Index	2Q12 A	1.50%	1.60%	2.00%
27-Jul	Core PCE QoQ	2Q12 A	1.80%	1.90%	2.30%
27-Jul	U. of Michigan Consumer Sentiment	JULY	72.00	72.50	72.00

# Forecasts

	2011	2012	2013	2014
Real GDP (% SAAR)	1.7	2.3	2.2	2.5
CPI (YoY %)	3.2	2.5	2.2	2.4
CPI Core (YoY %)	1.7	1.9	1.8	1.9
Unemployment Rate (%)	9.0	8.2	7.8	7.4
Fed Target Rate (eop, %)	0.25	0.25	0.25	0.50
10Yr Treasury (eop, % Yield)	2.0	2.2	2.7	3.1
US Dollar/ Euro (eop)	1.31	1.25	1.31	1.31

Note: Bold numbers reflect actual data

Kim Fraser  
Kim.Fraser@bbvacompass.com

**BBVA** RESEARCH



2001 Kirby Drive, Suite 31, Houston, Texas 7701 | Tel.: +34 91 374 60 00 | [www.bbva.com](http://www.bbva.com)

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