

U.S. Economic Flash

Small Business Quarterly, 3Q12

- Leading credit indicators suggest neither tightening nor easing in 3Q12**

The neutral reading from our leading credit index indicates that small business funding will remain subdued in 3Q12. On balance, low small business funding costs are being offset by weak supply-side funding conditions such as higher short-term market funding and increased liabilities. In total, low interest rates will not be enough to overtake the regulatory uncertainty felt by many small businesses.

- Small Businesses highlighted throughout each party's presidential platform**

The struggling small business environment has become a cornerstone of each party's campaign platform. Small business stimulus underlies broad based job and wealth creation and entails lower political costs than alternatives. Democrats' approach to small business growth includes infrastructure investment, which could boost the overall economic potential of the US in the medium-to-long run. Additionally, Democrats favor the direct subsidization of targeted industries such as clean energy. Republicans, on the other hand, support a non-interventionist pro-growth agenda that targets small businesses through reduced taxes, deregulation and the clarification of existing regulation.

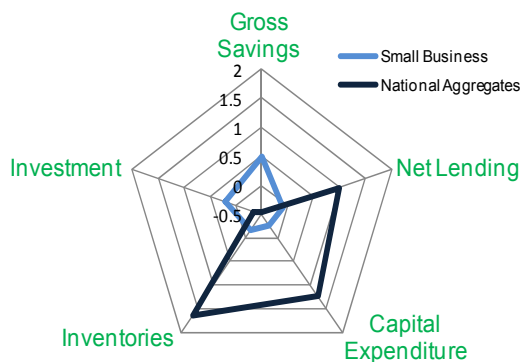
- Regulatory uncertainty loom over small business decision making**

The ongoing fiscal negotiations, impending fiscal cliff and unclear financial regulation are weighing on small business and lender confidence. The threat of fiscal contraction puts federal contractors in a precarious position: shutdown operations and wait for greater policy clarity or forge ahead at the risk of losing key funding for specific projects. As such, the defense, healthcare, energy and finance industries, which face the largest regulatory uncertainty, are likely to forgo large investments, thus dampening the hiring outlook. Thus, November's election outcome will be a key event to resolve today's heightened uncertainty.

- The BBVA Compass footprint tops list of most entrepreneurial states**

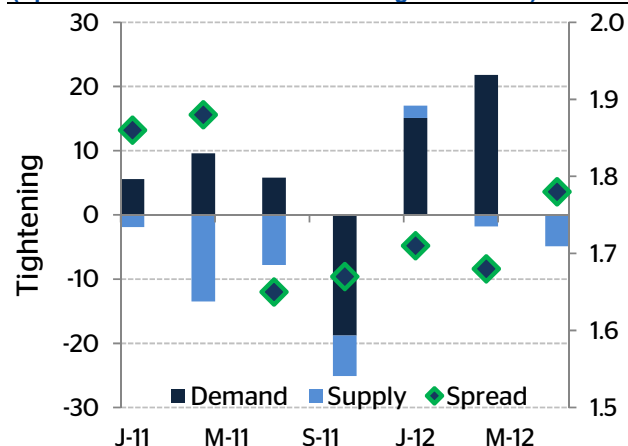
The Sunbelt remains a highly attractive environment for small businesses. Arizona, Texas, California and Colorado topped the list of most favorable states for entrepreneurial activity, according to the Kaufman Foundation. Florida rounded out the top ten, indicating that half of the most attractive small business environments in the U.S. lie within the BBVA Compass footprint. Attractive tax policies in Florida, Arizona and Texas, in addition to tech clusters in Colorado and California underlie this ranking.

Chart 1
Business Activity (QoQ change)



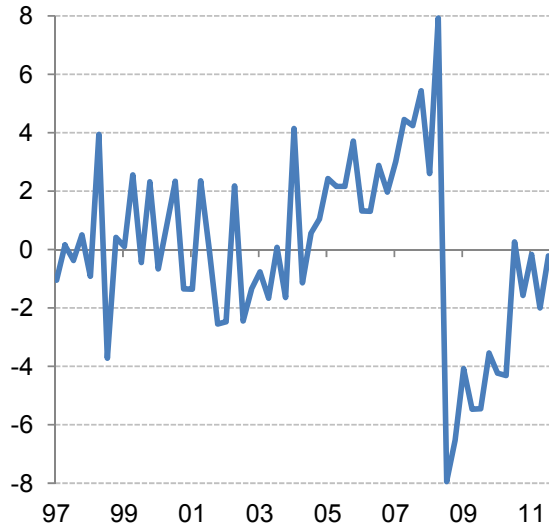
Source: Haver & BBVA Research

Chart 2
Credit Market Conditions and Small Business Spread (Spread: small Businesses rate vs Large firms rate)



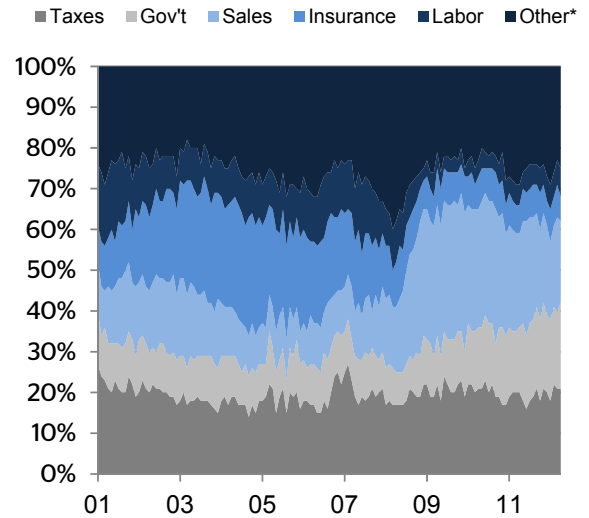
Source: Federal Reserve, Haver & BBVA Research

Chart 3
Small Business Leading Credit Index



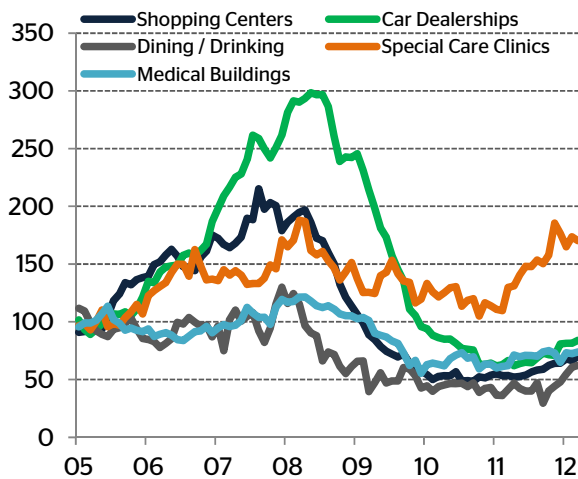
Source: Haver & BBVA Research

Chart 4
NFIB, Most Pressing Problems (% of respondents)



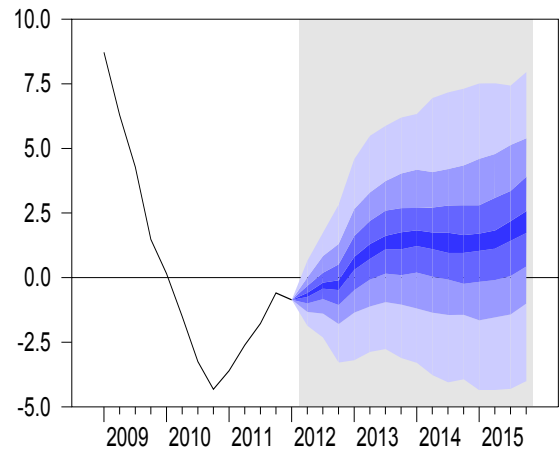
Source: Haver & BBVA Research
* Includes Large-firm competition, wages, interest rates, inflation and other

Chart 5
Construction Index (2005=100)



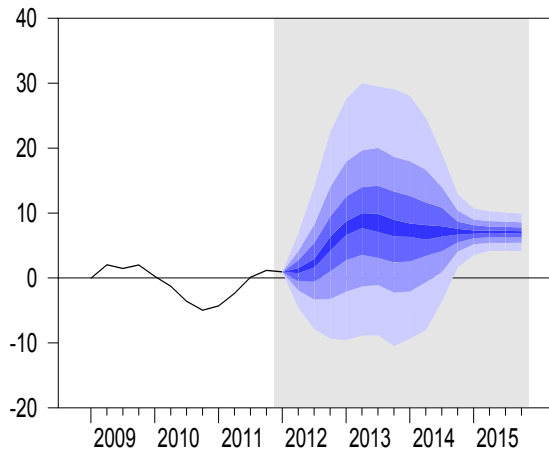
Source: Haver & BBVA Research

Chart 6
CRE Loan Forecasts, YoY % Change



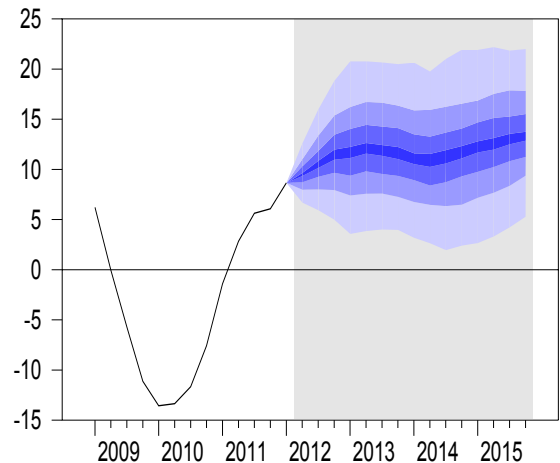
Source: Haver & BBVA Research

Chart 7
Trade Credit Forecasts, YoY % Change



Source: Haver & BBVA Research

Chart 8
Commercial and Industrial Loans, YoY % Change



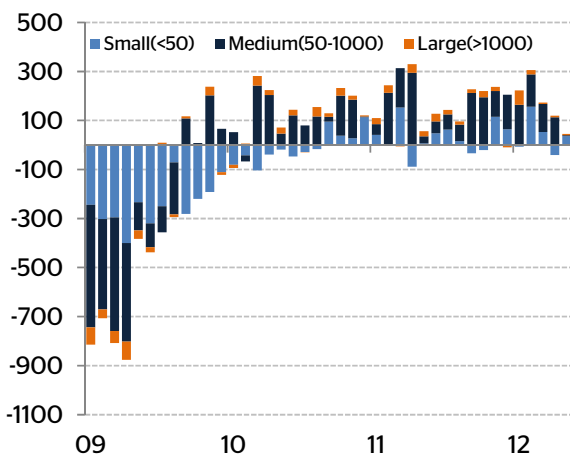
Source: Haver & BBVA Research

Small Business Employment Dynamics

Small businesses (less than 50 employees) have added 197K jobs since January 1st, although structural weaknesses suggest downside risks. For example, in May, total job creation was only 45K, and although small businesses accounted for 80% of that nationwide total, this pace is still far too low to reduce unemployment. Furthermore, the global slowdown, labor market weakness, an uncertain policy environment and misallocated credit markets weigh on small business confidence. Outside of the shock to uncertainty, charts 10 and 11 suggest increased job-skills mismatch; in essence, openings are accelerating whereas small business net job creation is stalled (chart 10). Given the aforementioned market headwinds, we believe that net job creation will remain tepid in spite of favorable borrowing costs.

Chart 9

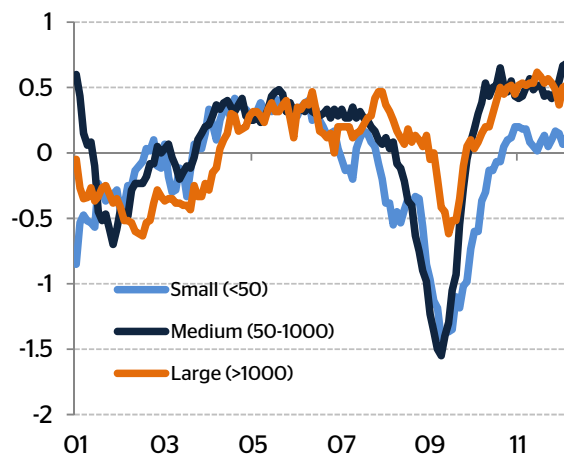
Employment Gap Contribution, k



Source: Haver & BBVA Research

Chart 10

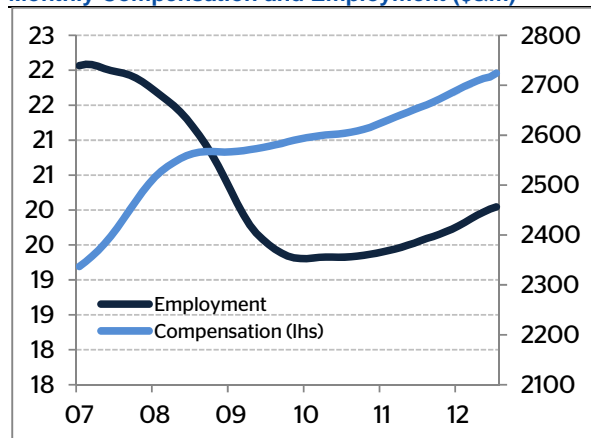
Net Job Creation Rate by Firm Size, 6mma (%)



Source: Haver & BBVA Research

Chart 11

Monthly Compensation and Employment (\$&m)*

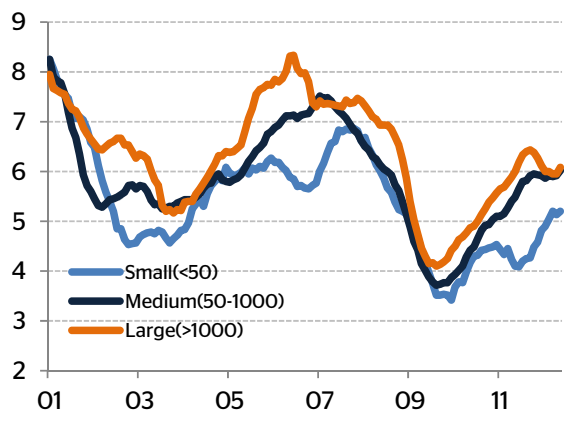


Source: Intuit & BBVA Research

*Small Business

Chart 12

Job Openings by Firm Size, 6mma (%)



Source: Haver & BBVA Research

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