

US Weekly Flash

Highlights

- **Unemployment drops to 7.7% with decline in labor force**

- Despite the surprising drop in the unemployment rate and the minimal reported impact of Hurricane Sandy, the November employment data should be taken with a grain of salt. Driving down the unemployment rate to 7.7% (the lowest since December 2008) was a simultaneous decline in the labor force, down 350K following two consecutive months of gains. According to data on the labor force status flows, more than 8% of employed workers dropped out of the labor force, while slightly less dropped out from unemployed status. This is likely a result of discouraged and long-term unemployed individuals leaving the workforce given that the number of those unemployed for 27 weeks and over declined more than 4% for the month. Similarly, the participation rate declined from 63.8% in October to 63.6% in November, while the employment-to-population ratio fell to 58.7%.
- Nonfarm payroll growth was relatively strong for November, beating consensus expectations for a modest 80K increase on pessimistic expectations for Sandy's impact. Overall payrolls increased 146K for the month, with private hiring up 147K. However, the figures for the past two months were also revised down fervently by 49K which makes the additions for November a little less robust than they seem. In general, the BLS reported little impact from the storm given the overlap between months, but the household survey did note a significant jump in the number of people "unable to work due to weather."
- Those who are employed saw their average workweek remain the same as in October but wage inflation rose slightly, up 0.2% after no change in the previous month. This increase is not enough however, to support sustainable job growth in the coming months and with the fiscal cliff only weeks away, it is likely December and early 2013 will see mixed reports across the board in terms of employment. The volatile changes in the labor force population also imply underlying weakness in employment sustainability

- **Manufacturing activity contracts as services expand in November**

- Far below economists' estimates, the ISM Manufacturing Index fell to its lowest level since 2009. Dropping to 49.5, the ISM in some aspects reflects the impact of Hurricane Sandy that devastated the East Coast and hindered both production and demand. This is most heavily reflected in the plunge in new orders from 54.2 to 50.3. Although still in expansionary territory, new orders have shrunk considerably in November as businesses dealt with restarting their production post-Sandy while the less-affected firms still hesitate to make purchases prior to fiscal policy action. This slowing domestic demand is paired with declining foreign demand as Europe has yet to stabilize enough to demand more goods from the U.S. and China is plagued by the same sluggish recovery.
- A more cautious view on future demand may also explain the fall in inventories as companies determine the risks behind over-production based on lack luster demand. Overall, the ISM's fall into contractionary territory should be temporary as Sandy's impact dwindles over the coming weeks and December figures perk up slightly. However, until U.S. fiscal policy is clear and European and Asian demand recovers, we do not expect the ISM index to recover quickly
- On the other hand, the ISM Non-Manufacturing Index accelerated slightly from 54.2 in October to 54.7 in November with a large push from overall business activity and new orders. The employment component was the weakest, falling to 50.3 and marking the lowest point since July. According to the ISM indices, the services sector has been faring much better than manufacturing throughout the past year, with the gap widening in the last six months. However, we expect that businesses in both sectors will be cautious entering 2013 as the effects of various fiscal reforms (or lack thereof) are realized.

Week Ahead

U.S. Trade Balance (October, Tuesday 8:30 ET)

Forecast: -\$42.8B	Consensus: -\$42.7B	Previous: -\$41.5B
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The trade deficit is expected to increase in October after falling to a two-year low in September. The third quarter closed on stronger-than-expected export growth, mostly related to petroleum products. However, various business surveys have noted a slowing in both export and import demand as we moved into the fourth quarter. Demand from our largest trading partners, despite last September's increase and a weaker dollar, doesn't seem sustainable given the downward pressures on global growth. With the holiday season approaching, October's figures could reflect rising domestic demand and business needs to import consumer goods. Import prices increased slightly in October and could push the nominal value slightly above that of exports, resulting in a slight worsening of the trade balance. Still, the increasing anxiety as the fiscal cliff approaches will surely keep trade levels subdued throughout 4Q12.

Retail Sales, Ex Auto (November, Thursday 8:30 ET)

Forecast: 0.3%, 0.2%	Consensus: 0.4%, 0.0%	Previous: -0.3%, 0.0%
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Retail sales are expected to rebound slightly in November as the Northeast recovers from the storm and consumers get geared up for the holiday season. As Sandy's impact becomes realized we await its lasting effects throughout indicators. Since retail sales are not restricted to the East alone, demand throughout the nation should fuel a turnaround in sales despite the lingering damage from Sandy. Auto and truck sales have increased in November which should lift retail sales slightly as parts and features are purchased. In addition, the post-Thanksgiving sales should boost retail spending for November as many shoppers spent hours queued in order to nab some early holiday gifts. Unfortunately, the impending fiscal cliff situation has impacted business and consumer confidence nationwide and the uncertainty could limit significant gains in sales for the month.

Consumer Price Index, Core (November, Friday 8:30 ET)

Forecast: -0.1%, 0.0%	Consensus: -0.2%, 0.2%	Previous: 0.1%, 0.2%
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The consumer price index is forecasted to drop slightly as commodity prices fall on average and the drought's effect on agricultural prices becomes less evident. Grain prices overall fell in November, impacting the price of feed which was in turn driving the price of livestock and meats. In addition, energy prices, excluding natural gas, have been declining in November, putting downward pressure on headline inflation. Although the rise in natural gas muffled the decline in oil prices, WTI and Brent crude oil prices may have edged down far enough to outweigh the rise in natural gas. Shelter may be an upward force for core inflation but the increase has been steady and November's figures don't purport much of a push from home prices. There is also little pressure in terms of wages, further evidencing the subdued consumer inflation figures for November.

Industrial Production (November, Friday 9:15 ET)

Forecast: 0.3%	Consensus: 0.2%	Previous: -0.4%
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Industrial production was hit hard in October as Hurricane Sandy shut down businesses for several days toward the end of the month. Despite various economic indicators noting a negative spillover to November, manufacturing surveys have reported increasing production for the month. The production component of the ISM accelerated in November despite a decline in the overall index, while the production jump in the Chicago survey may indicate strength in areas that were unaffected by the storm. Auto sales did jump significantly in November and could signal a positive contribution to the production figure. Overall we expect there to be an increase in the production data based on the recovering Northeast along with nationwide manufacturing and production increases.

Market Impact:

This week has a number of leading indicators that are worth paying attention to. The magnitude of the U.S. trade deficit is the first and may tell us how imports are fairing and whether demand globally for U.S. goods is shrinking. Retail sales should give us a glimpse into how businesses are doing now that Sandy's effects are waning and the holiday season arrives. Inflation data is not expected to send markets into a frenzy, particularly with most of the focus on the FOMC meeting announcement on Wednesday. Overall, we expect some good news out of next week but with the fiscal cliff deadline only weeks away it is unlikely next week will spur any calm.

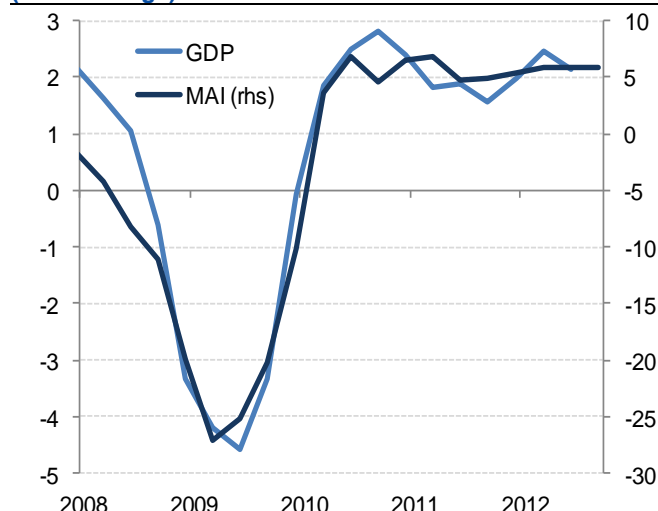
Economic Trends

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



Source: BBVA Research

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



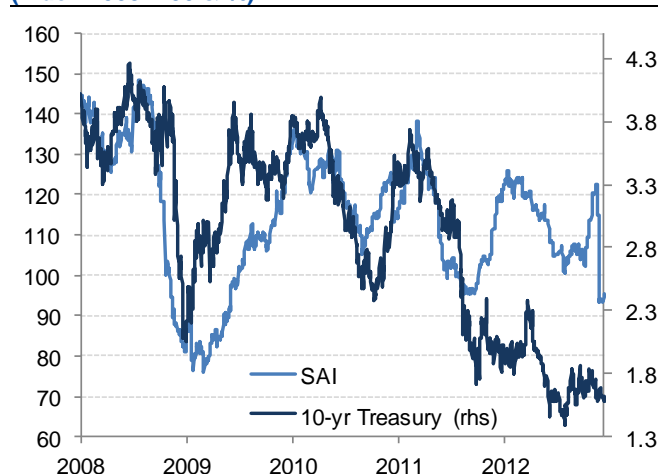
Source: BBVA Research & BEA

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



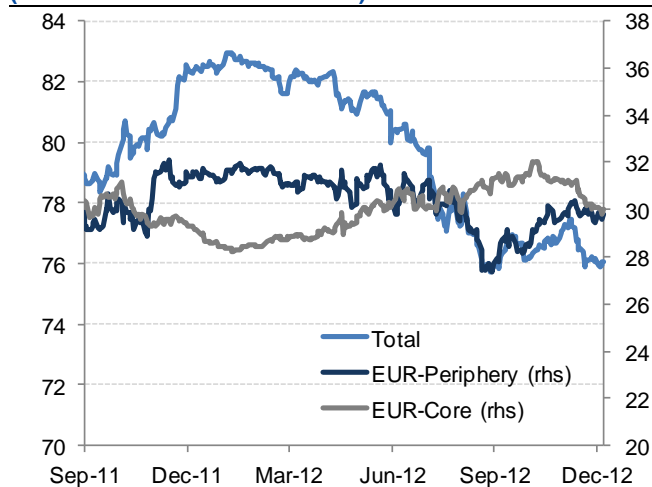
Source: BBVA Research

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



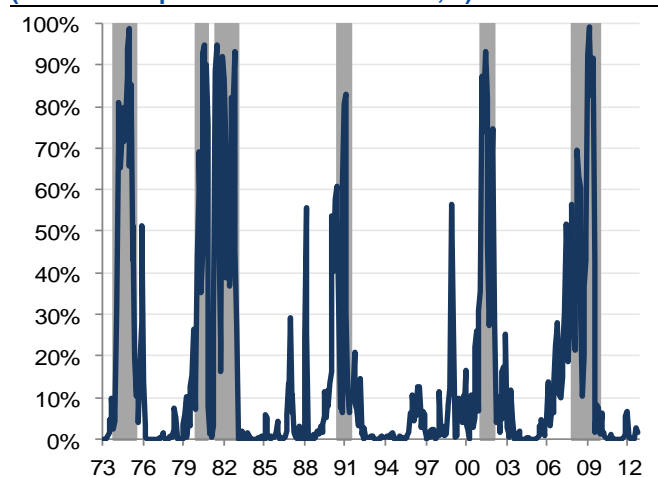
Source: Bloomberg & BBVA Research

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



Source: BBVA Research

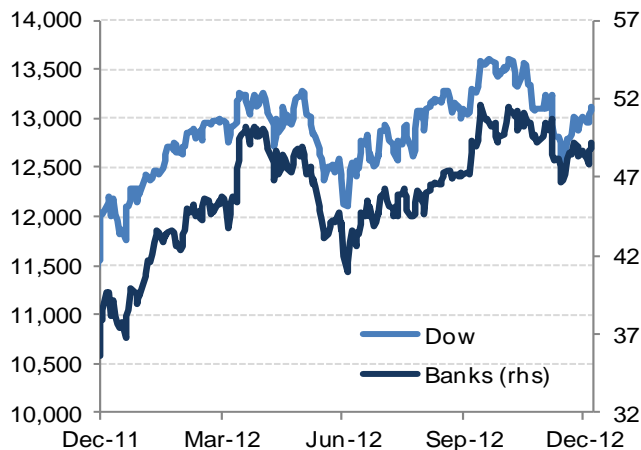
Graph 8
**BBVA US Recession Probability Model
(Recession episodes in shaded areas, %)**



Source: BBVA Research

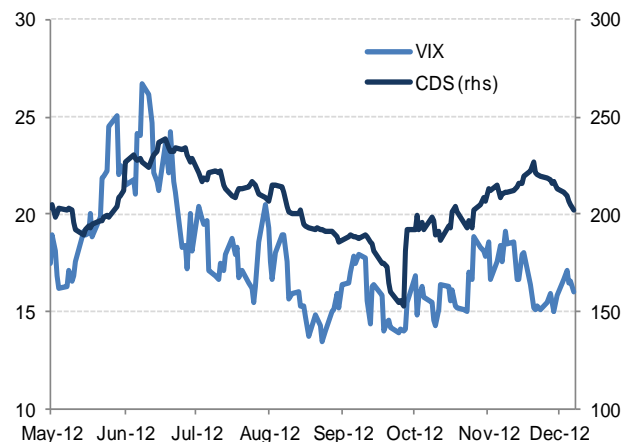
Financial Markets

Graph 9
Stocks
(Index, KBW)



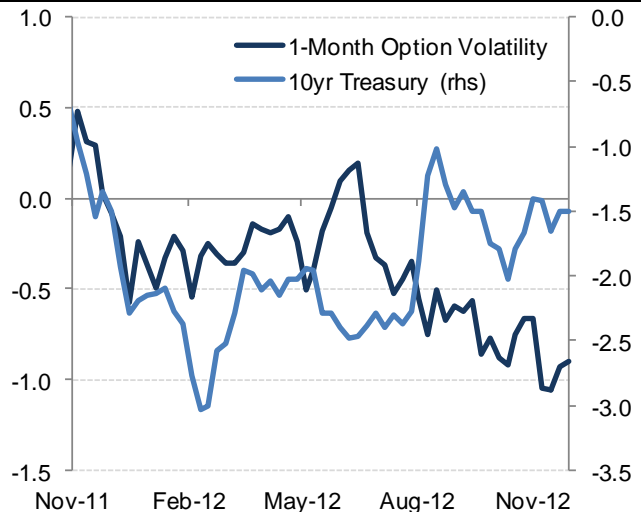
Source: Bloomberg & BBVA Research

Graph 10
Volatility & High-Volatility CDS
(Indices)



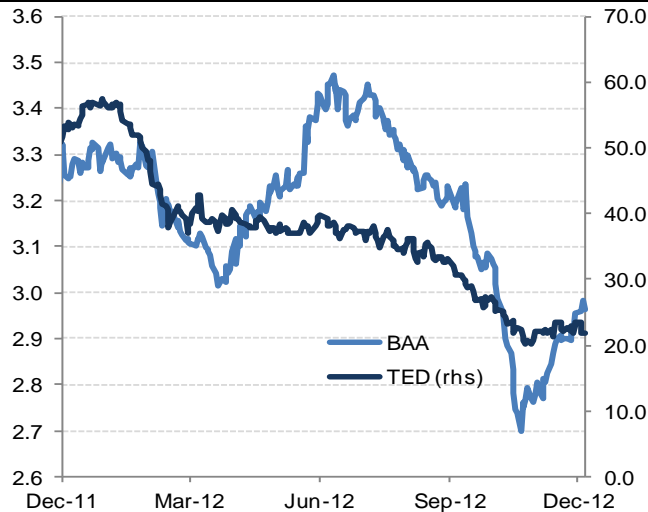
Source: Bloomberg & BBVA Research

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



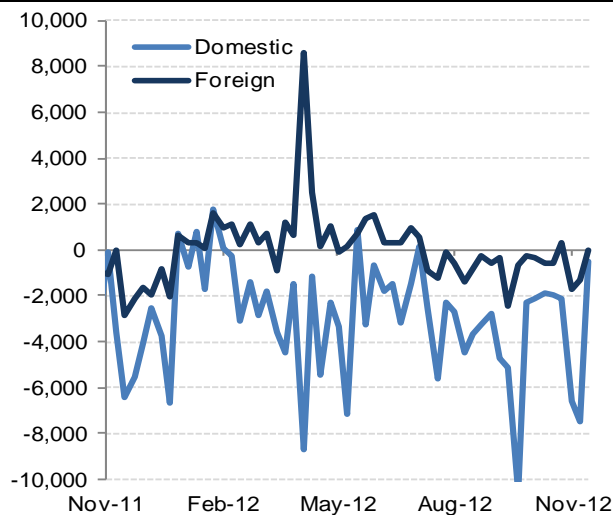
Source: Haver Analytics & BBVA Research

Graph 12
TED & BAA Spreads
(%)



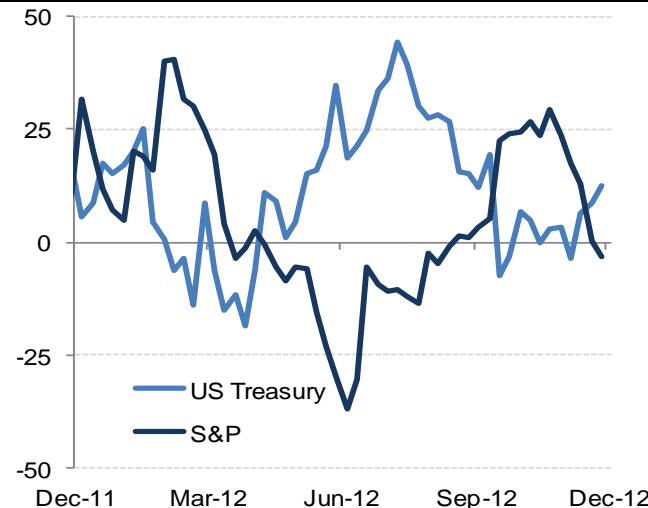
Source: Bloomberg & BBVA Research

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



Source: Haver Analytics & BBVA Research

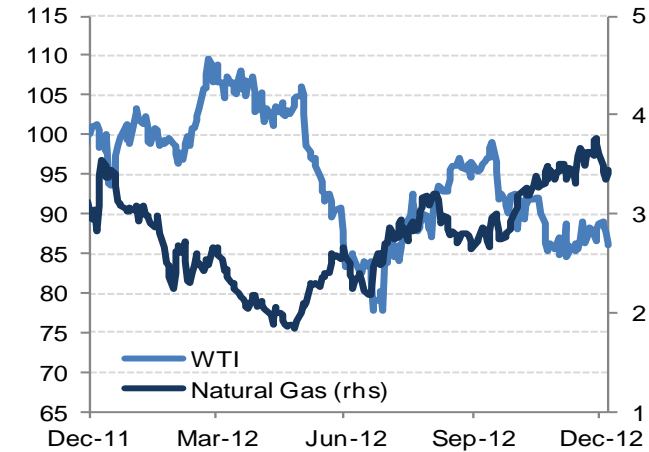
Graph 14
Total Reportable Short & Long Positions
(Short-Long, K)



Source: Haver Analytics & BBVA Research

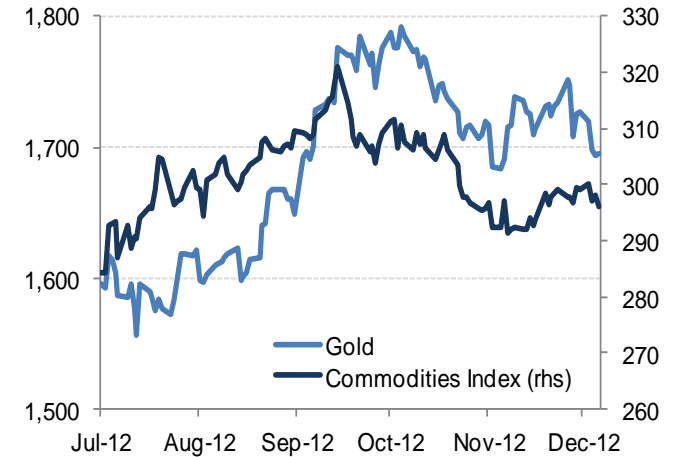
Financial Markets

Graph 15
Commodities
(Dpb & DpMMBtu)



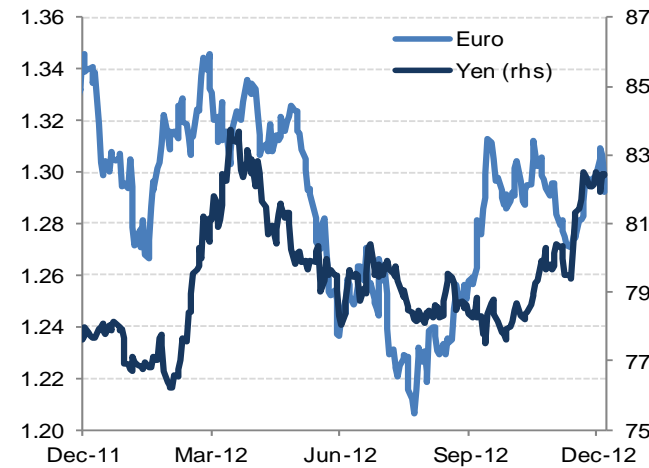
Source: Bloomberg & BBVA Research

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



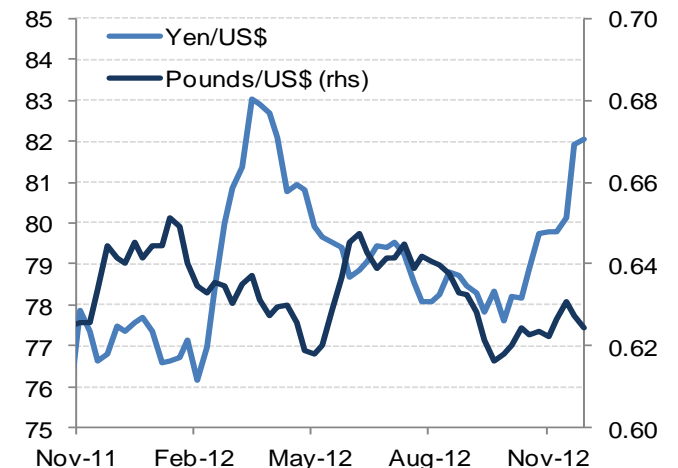
Source: Haver Analytics & BBVA Research

Graph 17
Currencies
(Dpe & Ypd)



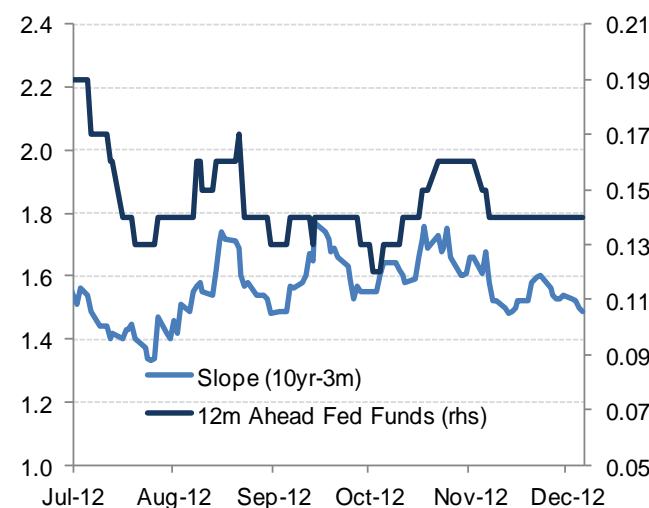
Source: Bloomberg & BBVA Research

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



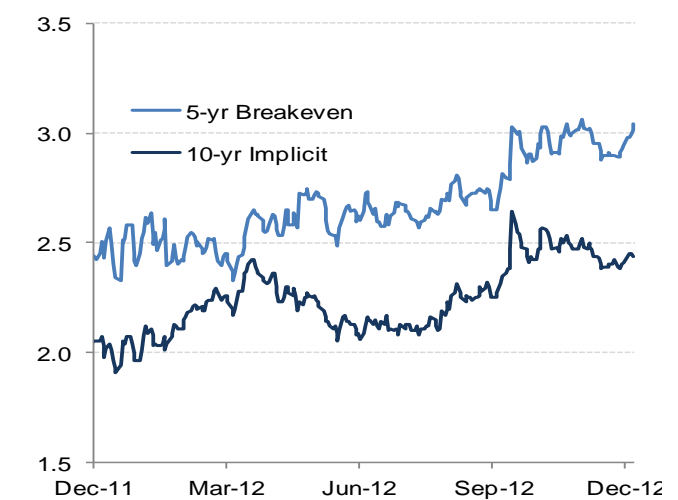
Source: Haver Analytics & BBVA Research

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)	13.98	13.98	14.12	13.94
New Auto (36-months)	2.78	2.78	3.07	3.76
Heloc Loan 30K	5.40	5.39	5.41	5.52
5/1 ARM*	2.69	2.72	2.73	2.93
15-year Fixed Mortgage *	2.67	2.64	2.69	3.27
30-year Fixed Mortgage *	3.34	3.32	3.40	3.99
Money Market	0.51	0.51	0.50	0.51
2-year CD	0.87	0.87	0.86	0.95

*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	0.16	0.16	0.16	0.07
3M Libor	0.31	0.31	0.31	0.54
6M Libor	0.52	0.53	0.53	0.76
12M Libor	0.85	0.86	0.86	1.08
2yr Sw ap	0.35	0.37	0.38	0.65
5yr Sw ap	0.75	0.75	0.77	1.26
10Yr Sw ap	1.68	1.66	1.65	2.19
30yr Sw ap	2.59	2.58	2.48	2.78
7day CP	0.14	0.32	0.17	0.75
30day CP	0.18	0.15	0.20	0.58
60day CP	0.20	0.19	0.20	0.47
90day CP	0.21	0.22	0.20	0.49

Source: Bloomberg & BBVA Research

Quote of the Week

Alan Greenspan, Former Chairman of the Federal Reserve
Interview with Bloomberg Surveillance
6 December 2012

"The presumption that we're going to have a painless solution to this [fiscal cliff], I think, is fantasy...there are a lot of risks out there but the one thing I can be reasonably certain of is we won't get through this whole issue without some pain."

Economic Calendar

Date	Event	Period	Forecast	Survey	Previous
11-Dec	International Trade Balance	OCT	-\$42.8B	-\$42.7B	-\$41.5B
11-Dec	Wholesale Inventories	OCT	0.3%	0.4%	1.1%
12-Dec	Import Prices (MoM)	NOV	-0.3%	-0.5%	0.5%
12-Dec	Export Prices (MoM)	NOV	-0.1%	-	0.0%
12-Dec	FOMC Meeting Announcement	DEC	0.25%	0.25%	0.25%
13-Dec	Advance Retail Sales	NOV	0.30%	0.40%	-0.30%
13-Dec	Retail Sales Less Autos	NOV	0.20%	0.00%	0.00%
13-Dec	Producer Price Index (MoM)	NOV	-0.30%	-0.50%	-0.20%
13-Dec	PPI Ex Food & Energy (MoM)	NOV	0.10%	0.20%	-0.20%
13-Dec	Initial Jobless Claims	8-Dec	365K	370K	370K
13-Dec	Continuing Claims	1-Dec	3190K	3215K	3205K
13-Dec	Business Inventories	OCT	0.4%	0.3%	0.7%
14-Dec	Consumer Price Index (MoM)	NOV	-0.10%	-0.20%	0.10%
14-Dec	CPI Ex Food & Energy (MoM)	NOV	0.00%	0.20%	0.20%
14-Dec	Industrial Production	NOV	0.3%	0.2%	-0.4%
14-Dec	Capacity Utilization	NOV	78.30%	78.00%	77.80%

Forecasts

	2011	2012	2013	2014
Real GDP (% SAAR)	1.8	2.1	1.8	2.3
CPI (YoY %)	3.2	2.0	2.1	2.4
CPI Core (YoY %)	1.7	2.1	1.9	2.0
Unemployment Rate (%)	9.0	8.1	8.0	7.6
Fed Target Rate (eop, %)	0.25	0.25	0.25	0.25
10Yr Treasury (eop, % Yield)	2.0	1.7	2.4	2.7
US Dollar/ Euro (eop)	1.32	1.25	1.31	1.31

Note: Bold numbers reflect actual data

Kim Fraser
Kim.Fraser@bbvacompass.com

Alejandro Vargas
Alejandro.Vargas@bbvacompass.com



| 2001 Kirby Drive, Suite 31, Houston, Texas 7701 | Tel.: +1 713 831 7345 | www.bbva.com

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