BBVA | RESEARCH

Economic Watch

United States

Houston, June 3, 2013
Economic Analysis

Kim Fraser
kim.fraser@bbvacompass.com

Monthly US Outlook: June

Temporary Slowdown Paves the Way for a Stronger Recovery

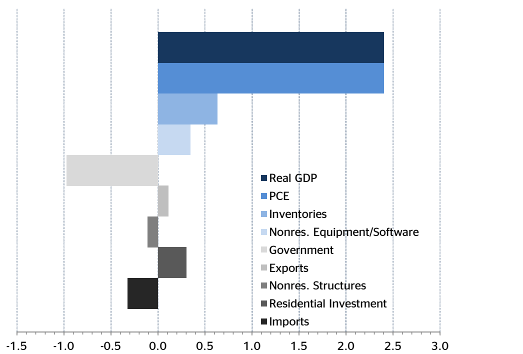
The second quarter is starting out just as we expected, with slow but steady activity pushing toward an acceleration in the latter half of 2013. Businesses and consumers alike are seeing a lagged impact from January's fiscal changes, but we expect that both will emerge from this 2Q13 lull as the year progresses. First quarter growth was relatively strong compared to the end of 2012 but the underlying details foreshadow slowing trends for the short-term. Real GDP growth stands at 2.4% QoQ SAAR, led mostly by personal consumption expenditures (PCE) and private inventory investment. While strong residential investment continues to reflect the ongoing housing recovery, nonresidential fixed investment slowed significantly in 1Q13, suggesting that businesses were anticipating quiet activity in 2Q13. Similarly, the rather modest import growth seen in the first quarter is indicative of the private sector's uncertainty when it comes to consumer demand throughout the next few months. Export growth was also extremely slow, surely not enough to recoup from 4Q12's decline, and supports our expectations for slowing activity on a global scale. Finally, it comes as no surprise that the government sector weighed on 1Q13 growth for the second consecutive quarter. We expect the sequester and other fiscal related issues to have the biggest impact on 2Q13 growth as the cuts to both federal and state/local spending continue to unfurl.

Personal consumption remains the bright spot in this consumer-driven recovery. Consumption growth accelerated to 3.4% QoQ SAAR in 1Q13, the fastest pace since 4Q10, on strong goods and services expenditures. Services expenditures made up the majority of total PCE growth for the first quarter as spending on housing and utilities spiked. Durable goods spending continues to be dominated by recreational goods, with the motor vehicles component often very volatile from quarter to quarter. Overall, PCE has remained the largest contributor to GDP throughout the past year as both private investment and net exports shrank. Aside from the projected slowdown in 2Q13, we expect that PCE will average close to 2.0% growth throughout the latter half of 2013 and into 2014 as we move toward more self-sustaining economic activity.

Other economic indicators for 2Q13 are supportive of a temporary slowdown. While real personal spending and retail sales remain mostly stable on an annual basis, monthly figures are a bit more disappointing. In particular, auto sales have dropped significantly in the past few months as consumers shied away from big ticket items. Similarly, both new and existing home sales have seen only modest improvements throughout 2013 thus far, though much of this is a consequence of constrained supply in the market. The demand is mostly there, especially with the threat of higher mortgage rates encouraging more immediate action from homebuyers. Rising home prices are likely to continue and should help alleviate some of the supply issues as current homeowners feel more comfortable putting their homes back on the market. Furthermore, continued improvements in the employment situation, as gradual as they may be, will surely boost consumer confidence when it comes to consumption. Inflation has also been supportive of a slow-growth environment in the short term. The latest CPI reports have noted declines in the headline figure for the past few months as energy pressures remain subdued. Core inflation has also moderated somewhat but we continue to see upward pressures from shelter and medical care services.

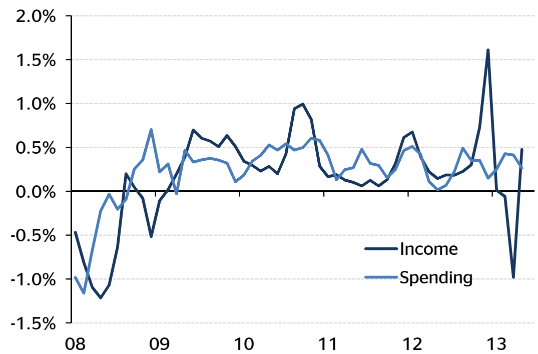
Of the domestic and global risks on our radar, fiscal policy remains one of the most uncertain factors. Despite the past few years of intense political brinkmanship leaving a sour mark on the public view, we are still not seeing any major efforts from either party to compromise. On par with the past few years, we can most likely expect the coming months to incite reoccurring political fissures that result in another "kick the can down the road" outcome.

Chart 1
Contributions to Real GDP Growth (1Q13 Preliminary, SAAR Percentage Points)



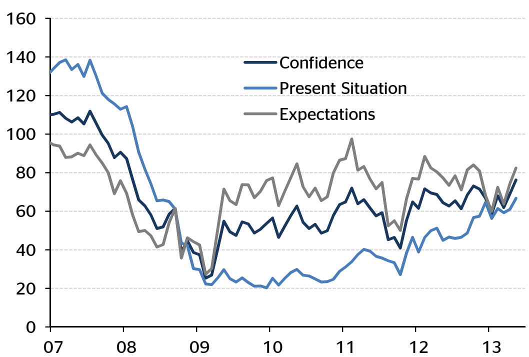
Source: BEA and BBVA Research

Chart 2
Personal Income and Expenditures (3MMA, MoM % Change)



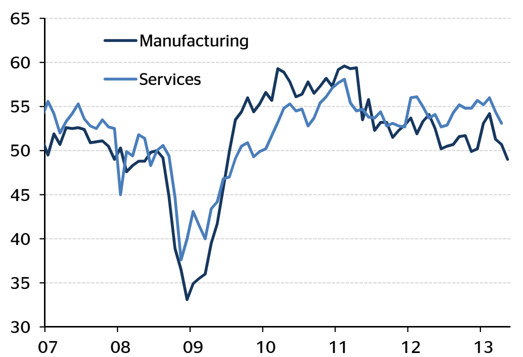
Source: BEA and BBVA Research

Chart 3
Consumer Confidence (SA, Index 1985=100)



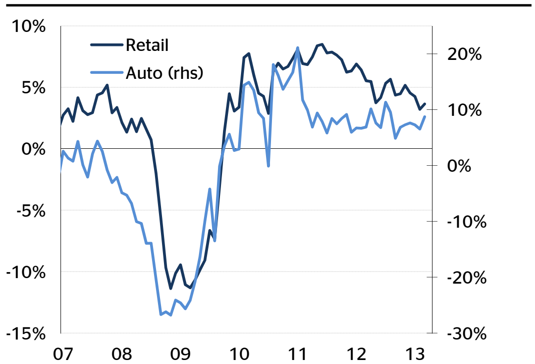
Source: Conference Board and BBVA Research

Chart 4
ISM Indices (SA, 50+= Expansion)



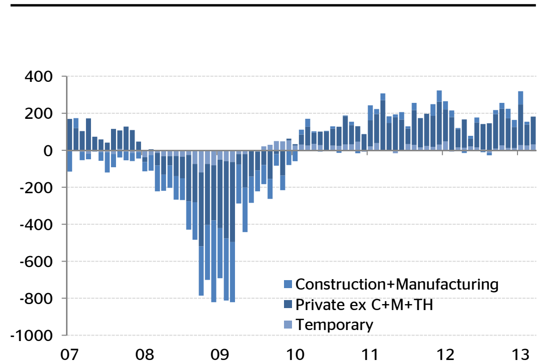
Source: ISM and BBVA Research

Chart 5
Retail and Auto Sales (YoY % Change)



Source: US Census Bureau and BBVA Research

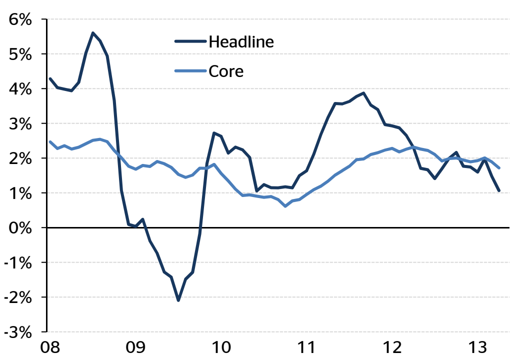
Chart 6
Private Nonfarm Payrolls (Monthly Change in K)



Source: BLS and BBVA Research

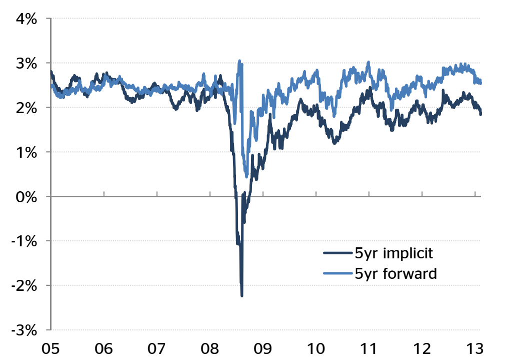
BBVA | RESEARCH

Chart 7
Consumer Price Index (NSA, YoY % Change, 1982-84=100)



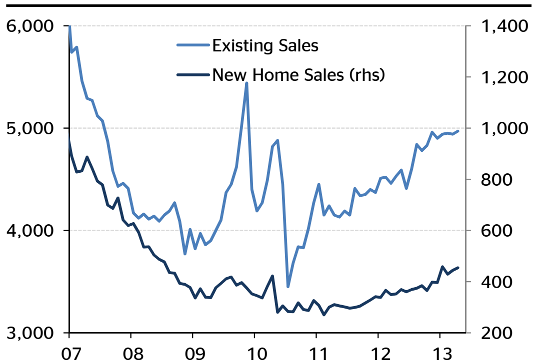
Source: BLS and BBVA Research

Chart 8
Inflation Expectations (%)



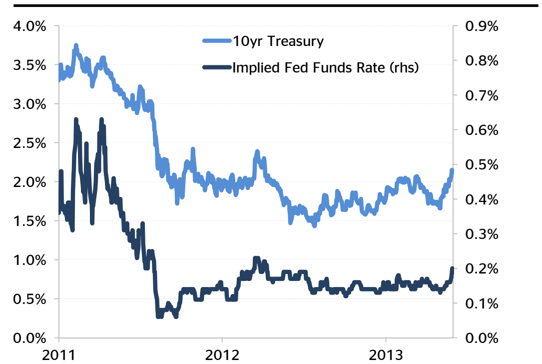
Source: Federal Reserve Board and BBVA Research

Chart 9
New and Existing Home Sales (Thousands, SAAR)



Source: US Census Bureau and BBVA Research

Chart 10
12-Month Implied Fed Funds Rate and 10-Yr Treasury (% Yield)



Source: Federal Reserve Board and BBVA Research

Table 1
Forecasts (BOLD=FORECASTS)

	2Q12	3Q12	4Q12	1Q13	2011	2012	**2013**	**2014**	**2015**
Real GDP (% SAAR)	1.3	3.1	0.4	2.4	1.8	2.2	**1.8**	**2.3**	**2.5**
Real GDP (Contribution, pp)									
PCE	1.1	1.1	1.3	2.4	1.8	1.3	**1.4**	**1.2**	**1.2**
Gross Investment	0.1	0.9	0.2	1.2	0.6	1.2	**0.8**	**1.0**	**1.1**
Non Residential	0.4	-0.2	1.3	0.2	0.8	0.8	**0.6**	**0.8**	**0.9**
Residential	0.2	0.3	0.4	0.3	0.0	0.3	**0.3**	**0.2**	**0.2**
Exports	0.7	0.3	-0.4	0.1	0.9	0.5	**0.3**	**0.9**	**0.9**
Imports	-0.5	0.1	0.7	-0.3	-0.8	-0.4	**-0.3**	**-0.9**	**-0.8**
Government	-0.1	0.8	-1.4	-1.0	-0.7	-0.3	**-0.5**	**0.1**	**0.1**
Unemployment Rate (%)	8.2	8.0	7.8	7.7	8.9	8.1	**7.5**	**7.0**	**6.5**
Average Monthly Nonfarm Payroll (K)	108	152	209	206	175	183	**164**	**193**	**219**
CPI (YoY %)	1.9	1.7	1.9	1.7	3.1	2.1	**2.0**	**2.2**	**2.3**
Core CPI (YoY %)	2.3	2.0	1.9	1.9	1.7	2.1	**1.9**	**2.0**	**2.1**
Fiscal Balance (% GDP)	-	-	-	-	-8.7	-7.0	**-4.1**	**-3.5**	**-2.3**
Current Account (bop, % GDP)	-3.0	-2.8	-2.8	-	-3.1	-3.1	**-2.9**	**-3.4**	**-3.5**
Fed Target Rate (%, eop)	0.25	0.25	0.25	0.25	0.25	0.25	**0.25**	**0.25**	**0.50**
S&P Case-Shiller Index	1.64	3.62	7.25	10.17	-4.38	2.78	**9.36**	**8.34**	**5.53**
10-Yr Treasury (% Yield, eop)	1.62	1.72	1.72	1.96	1.98	1.72	**2.30**	**2.73**	**3.39**
U.S. Dollar / Euro (eop)	1.25	1.29	1.31	1.30	1.31	1.31	**1.29**	**1.30**	**1.35**
Brent Oil Prices (dpb, average)	108.5	109.7	110.3	112.6	111.3	111.7	**108.0**	**112.9**	**119.0**

Source: BBVA Research