BBVA | RESEARCH

U.S. Economic Outlook

Monthly Update

June 11, 2014

BBVA | RESEARCH

Meeting Details

Topic: U.S. Monthly Economic Outlook
Date: Wednesday, June 11, 2014
Time: 10:00 am, Central Standard Time (Chicago, GMT-06:00)
Meeting Number / Access Code: 717 968 839
Meeting Password: bbva

To join the online meeting:
https://bbvacompass.webex.com/bbvacompass/j.php?MTID=m3ac541ae5090ddd76e5893b4ca263a32
To join the audio conference only:
Call-in toll-free number (US/Canada): 1-877-768-4036
Call-in toll number (US/Canada): 1-972-932-2100
Global call-in numbers:
https://bbvacompass.webex.com/bbvacompass/globalcallin.php?serviceType=MC&ED=187370482&tollFree=1

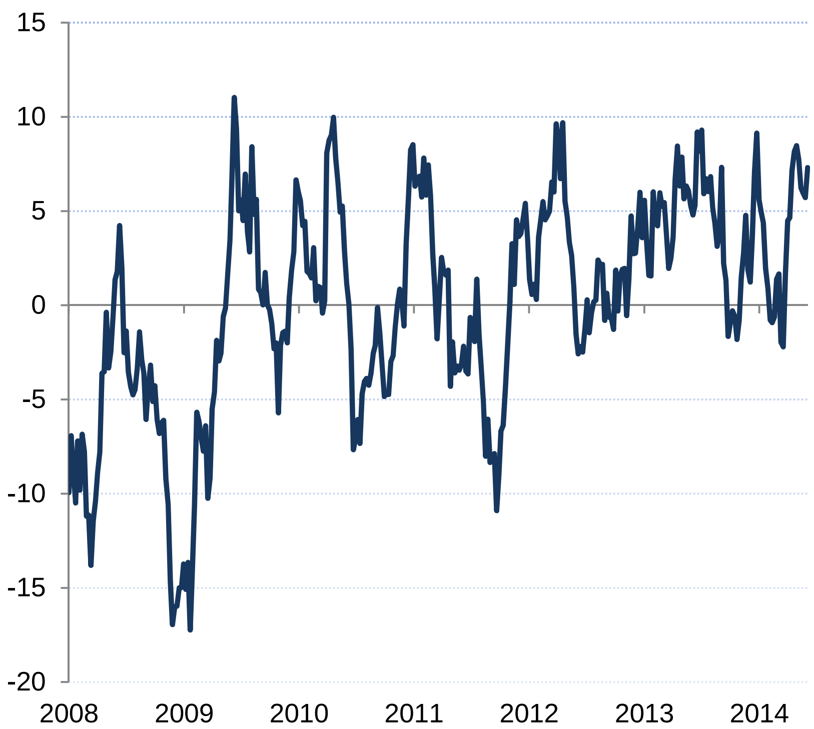
BBVA RESEARCH

Economic Activity

We expect an upward revision to 1Q14 GDP and a stronger pace of activity in coming quarters

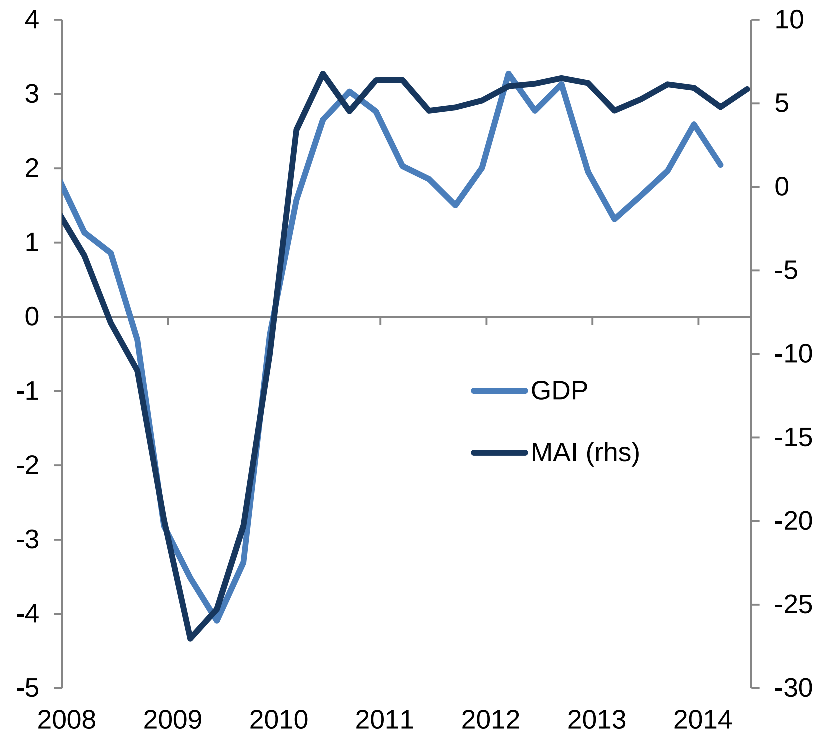
BBVA US Weekly Activity Index

3m % change



Real GDP Growth & Monthly Activity Index

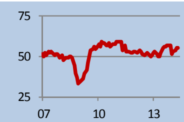
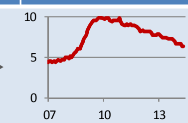
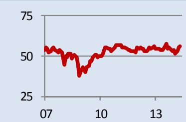
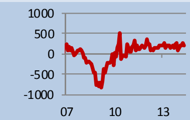
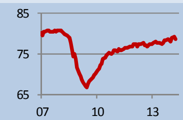
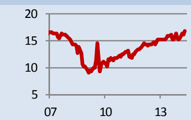
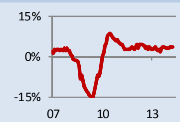
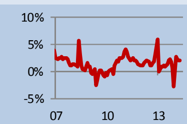
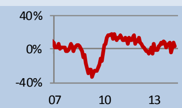
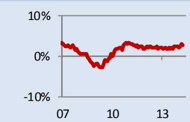
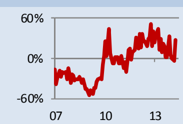
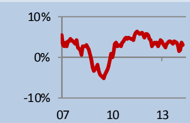
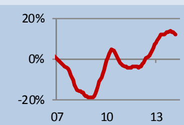
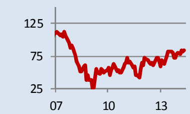
4Q % change



Source: BBVA Research

Economic Activity

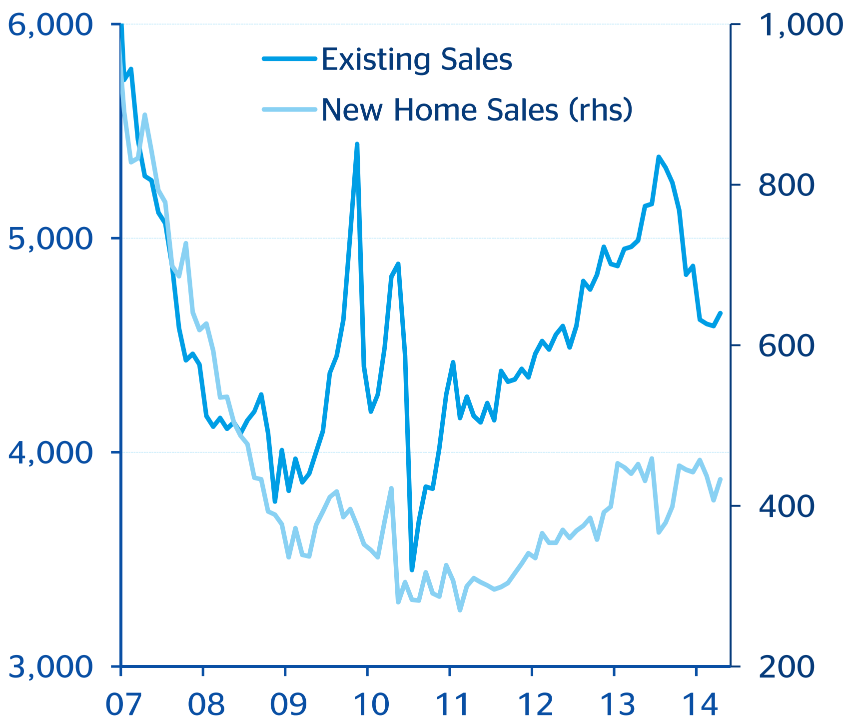
Spring rebound is more evident, but weaker global demand and some housing sector pressures are limiting the pace of expansion

Indicator	Assessment		Indicator	Assessment	
ISM Manufacturing	↗		Unemployment Rate (%)	→	
ISM Non-Manufacturing	↗		Nonfarm Payrolls (MoM Change in K)	→	
Capacity Utilization	→		Auto Sales (Millions)	↗	
Industrial Production (YoY % Change)	→		Real Disposable Income (YoY % Change)	→	
Capital Goods New Orders (YoY % Change)	→		Real Personal Spending (YoY % Change)	→	
Housing Starts (YoY % Change)	↗		Retail Sales Ex Auto & Gas (YoY % Change)	→	
Home Prices: S&P Case-Shiller (YoY % Change)	→		Consumer Confidence Index	↗	

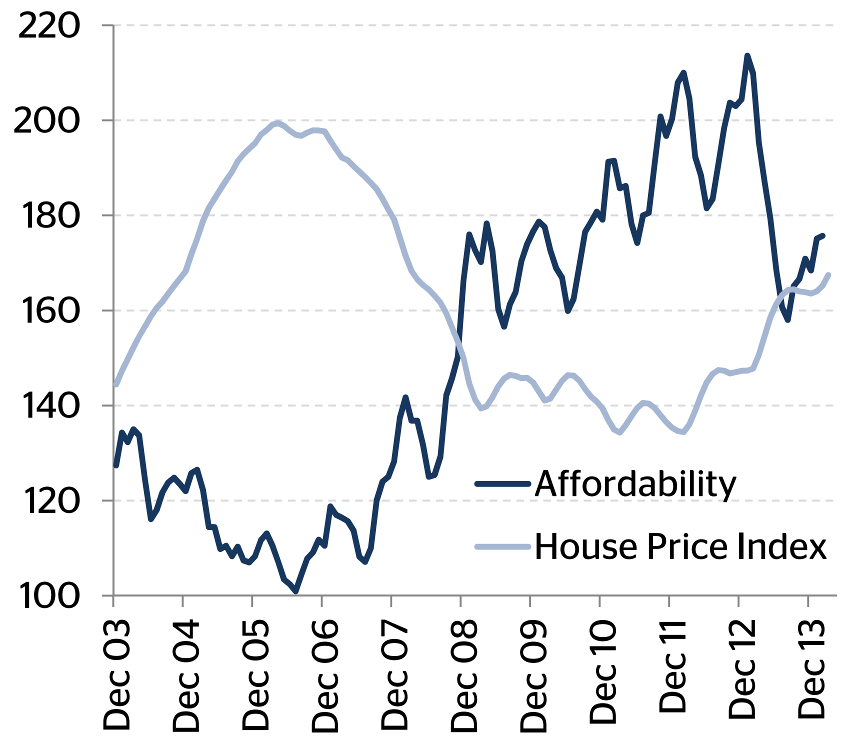
Residential Sector

Slower housing demand in response to weaker affordability due to higher interest rates & house prices.

Home sales
Thousands



House prices & Affordability
Index



Source: BBVA Research & Haver

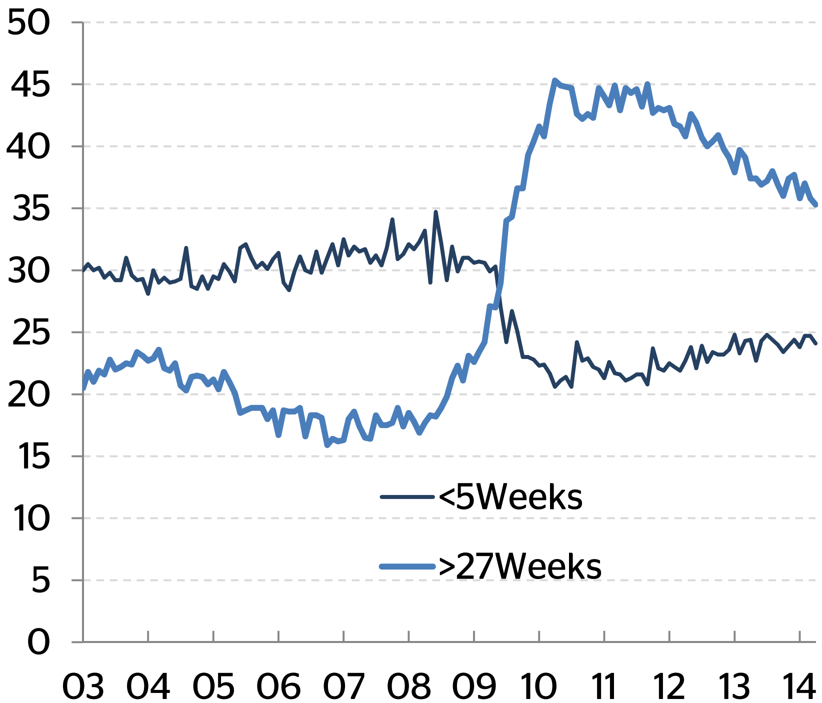
BBVA RESEARCH

Labor Markets

Despite the improvement in some labor market indicators, conditions remain weak

Duration of unemployment

% share



Bevereidge Curve

%

Source: BBVA Research & Haver

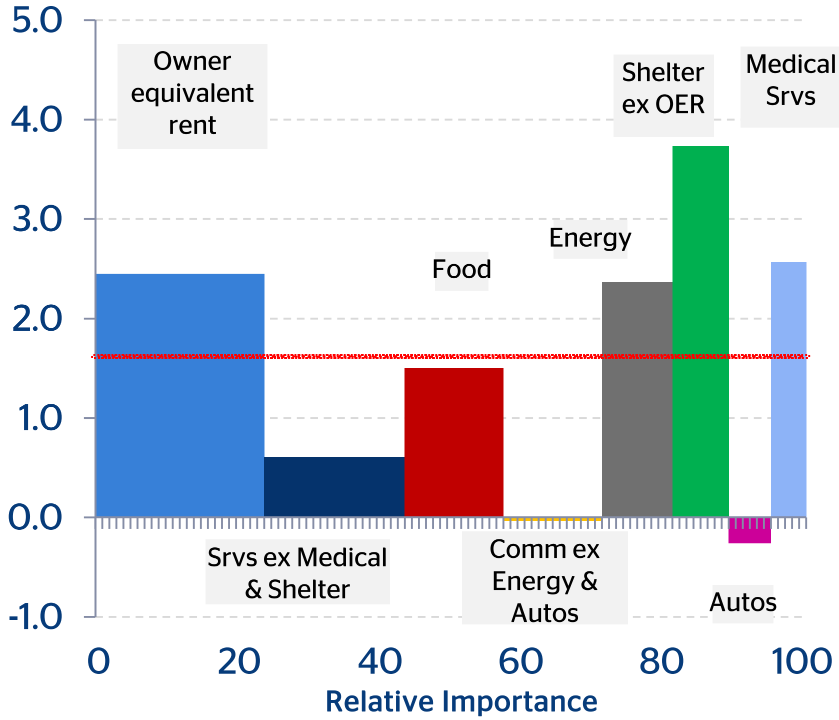
BBVA RESEARCH

Inflation

As expected, downward price pressures are easing

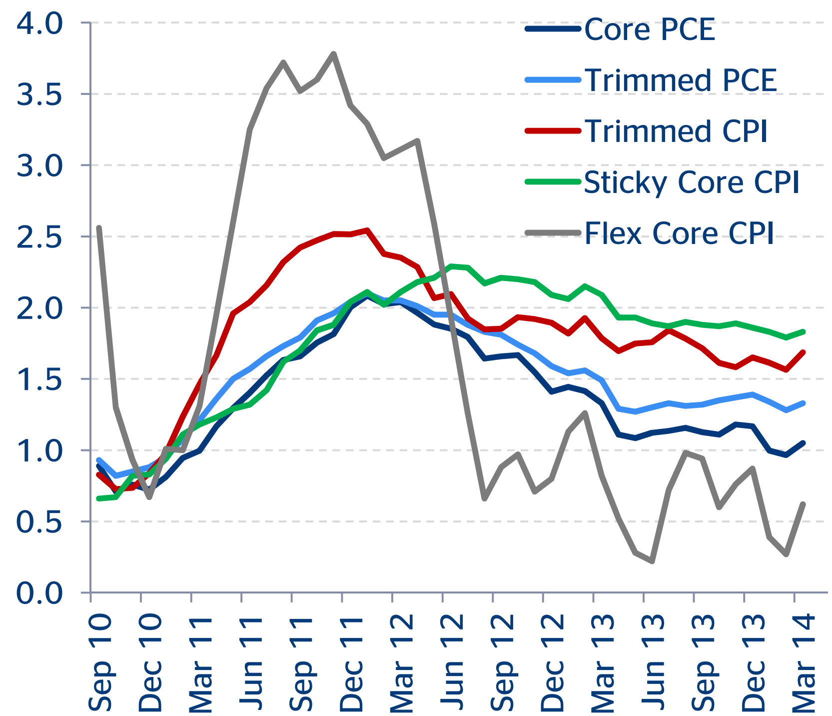
Contributions to CPI

Relative Importance & 12m% change



Inflation

12m % change



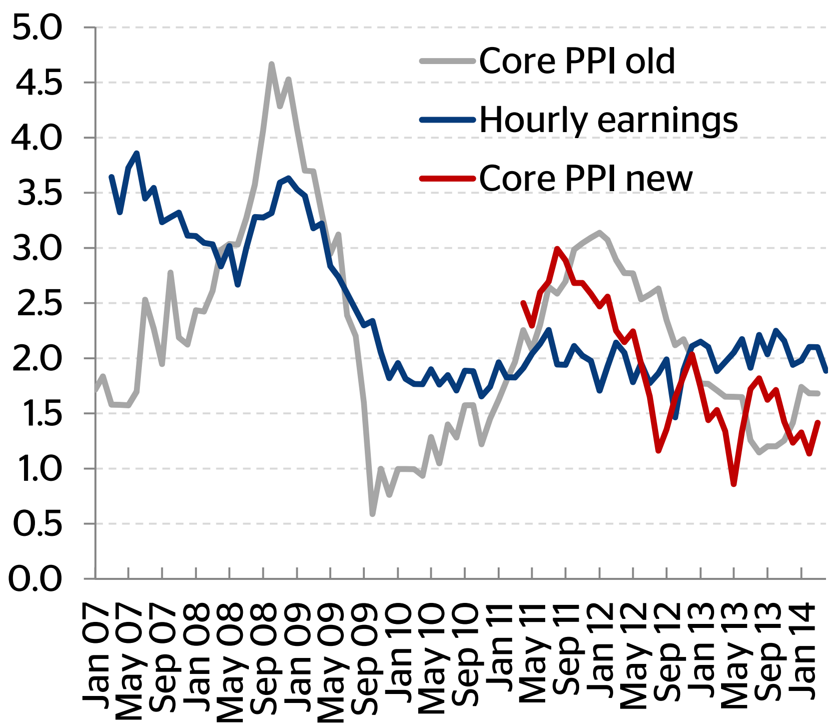
Source: BBVA Research / Haver

Inflation

However, inflation will remain at low levels

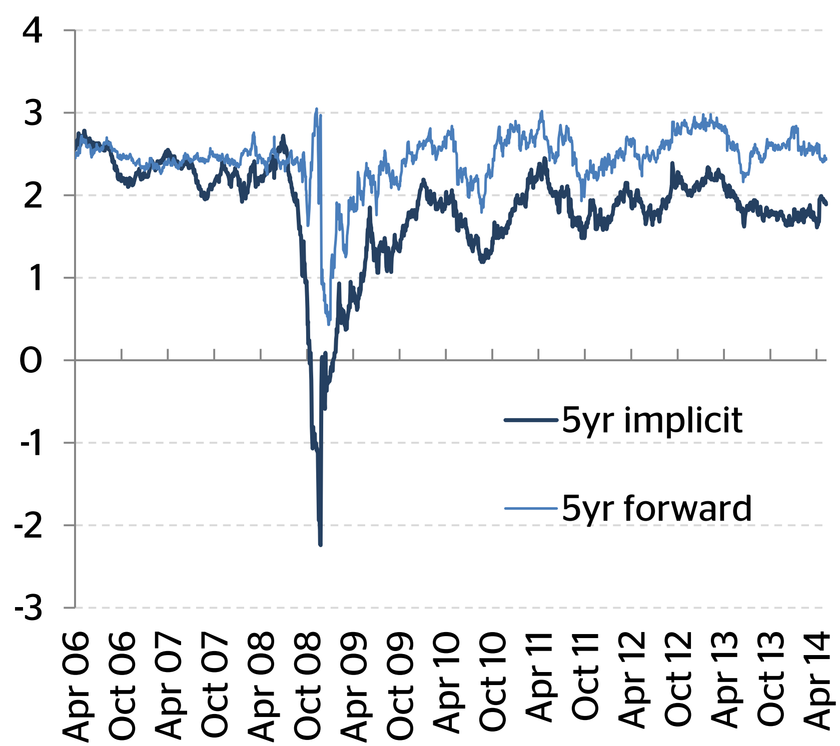
Producer Prices and Wage Costs

12m % change



Inflation Expectations

%



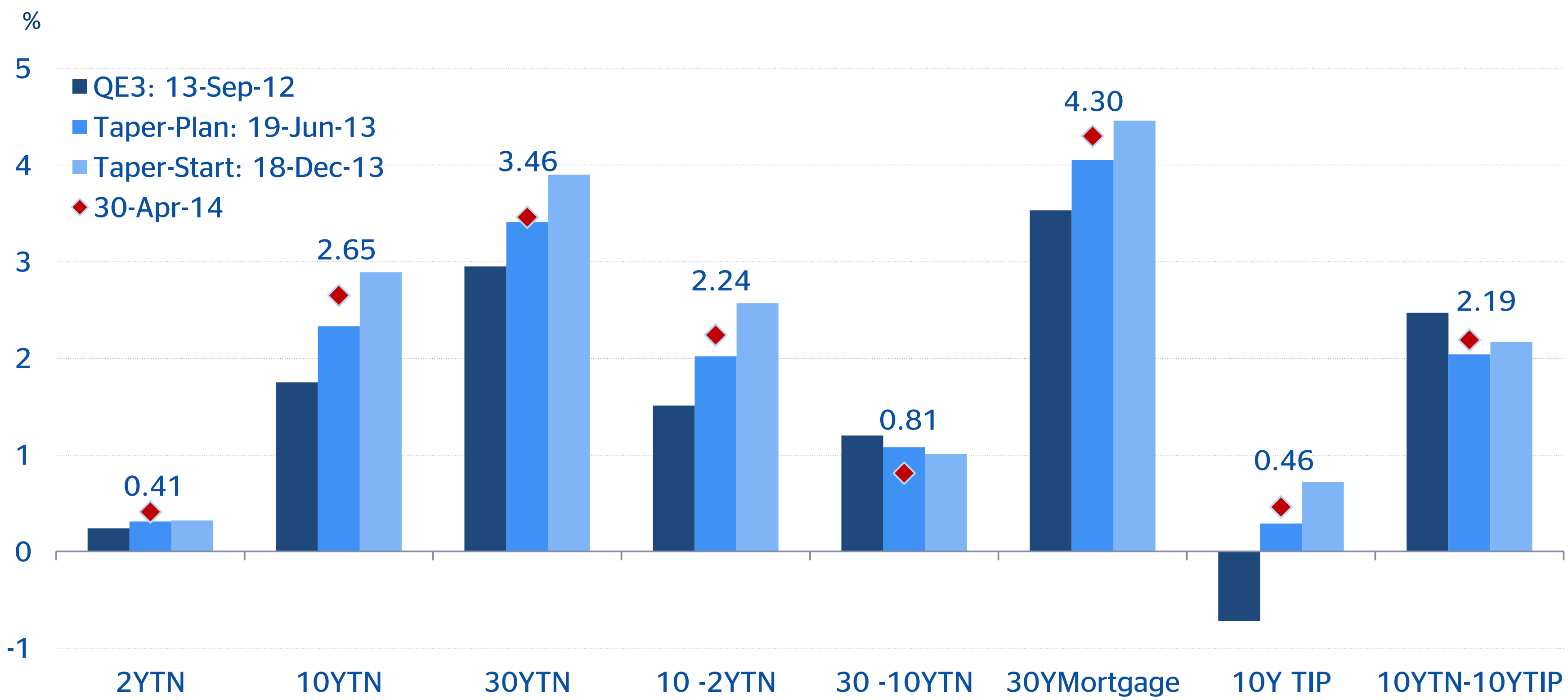
Source: BBVA Research / Haver

BBVA RESEARCH

Monetary Policy

No surprises in the latest FOMC meeting. We maintain our expectations for 4Q14 end to tapering and first rate hike in mid-2015

FOMC Announcement Impact on Interest Rates



Monetary Policy

Fed

Latest

Congressional Testimony: May 7, 2014

- Yellen's message remains dovish stating that "a high degree of monetary accommodation remains warranted"
- Reaffirmed that Fed is well prepared to the process of balance sheet normalization with new repo tools (overnight, term and reverse repos).
- However, no commitment to a preset course or timetable of Fed's exit
- Reassured that "valuations for the equity market as a whole and other broad categories of assets, remain within historical norms."

What do we expect?

- Measured steps of $10bn per month reduction of QE3
- Course of policy firming remains data dependent
- Anticipated changes to June projections on "pace of policy firming" due to new incoming FOMC members
- FOMC likely to introduce further modifications to the forward guidance to address the principal payments re-investment policy

Policy pause until

Mid - **2015**

Maintaining the 3Q15 baseline but with lower likelihood as the probability of an early rate hike has increased

Expected Timeline for Exit Strategy

4Q14
Expected End QE3

3Q15
First FFR Hike

1H16
Policy Normalization
Balance sheet: let securities mature/sales

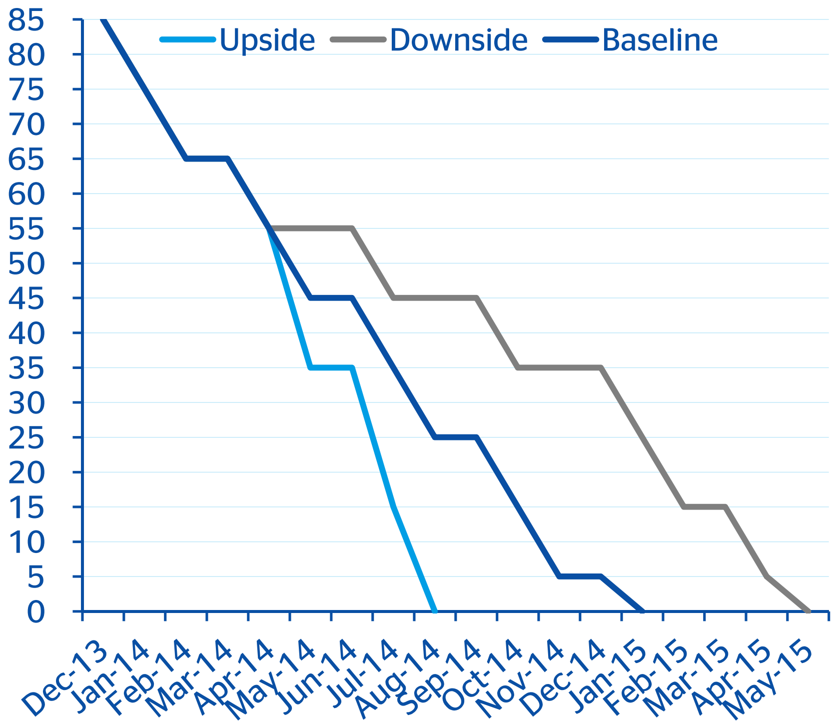
BBVA RESEARCH

Monetary Policy

Although we maintain our Fed funds scenario unchanged, the risks have tilted toward an earlier rate hike

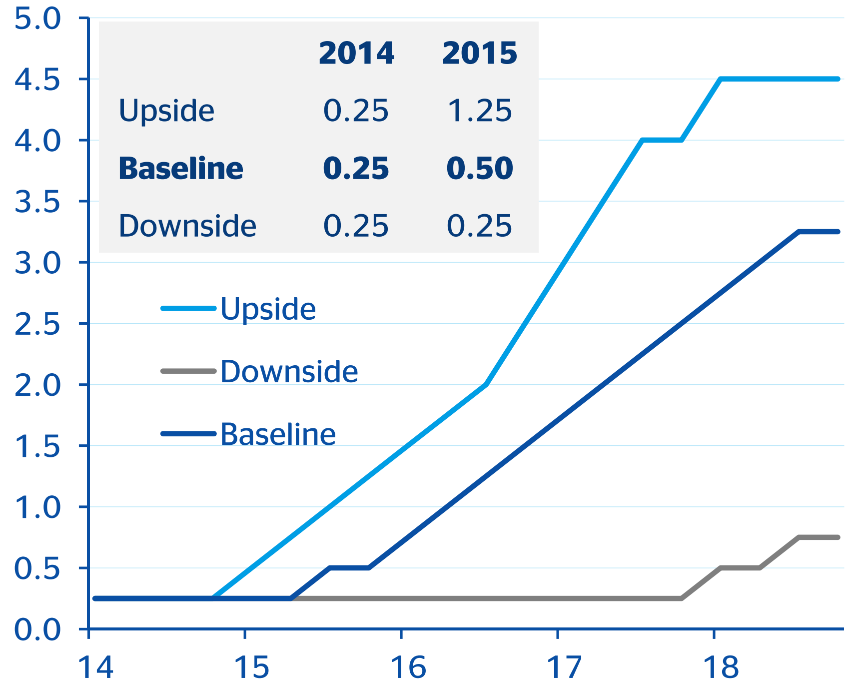
LSAP Tapering

US$bn



Federal Funds Rate Forecasts

%



	2014	2015
Upside	0.25	1.25
Baseline	**0.25**	**0.50**
Downside	0.25	0.25

Source: BBVA Research

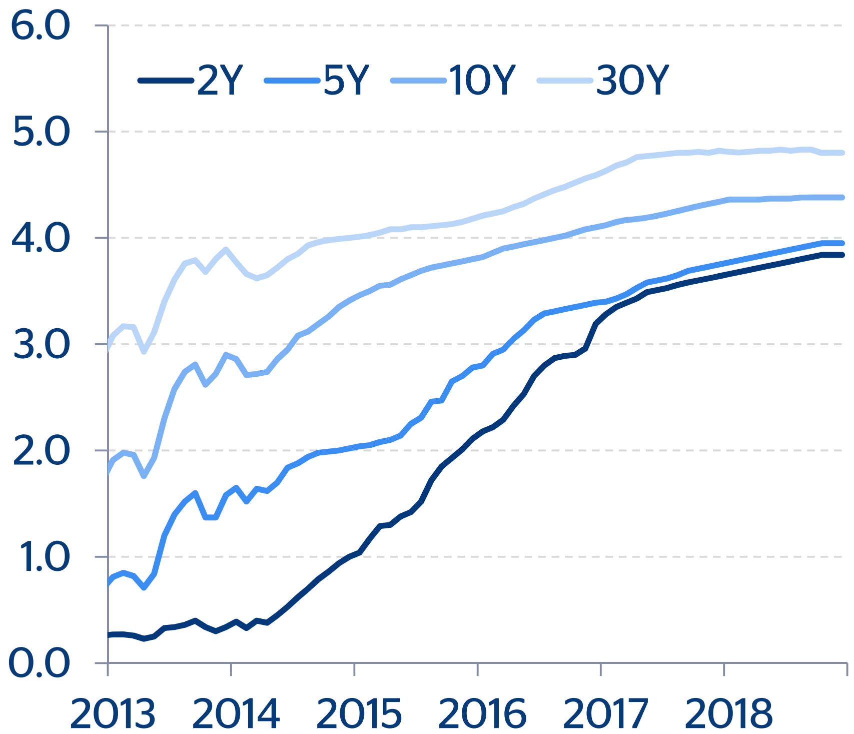
BBVA RESEARCH

Yield Curve

We maintain our forecasts unchanged

US Yield Curve: Official Scenario

%,



Yield Curve Slope 10YTN-2YTN

%

Source: BBVA Research

Baseline Forecasts

	1Q13	2Q13	3Q13	4Q13	1Q14	2011	2012	2013	**2014**	**2015**	**2016**	**2017**
Real GDP (% SAAR)	1.1	2.5	4.1	2.6	-1.0	1.8	2.8	1.9	**2.5**	**2.5**	**2.8**	**2.8**
Real GDP (Contribution, pp)												
PCE	1.5	1.2	1.4	2.2	2.1	1.7	1.5	1.4	**1.8**	**1.1**	**1.2**	**1.3**
Gross Investment	0.7	1.4	2.6	0.4	-2.0	0.7	1.4	0.8	**0.4**	**0.9**	**1.0**	**1.1**
Non Residential	-0.6	0.6	0.6	0.7	-0.2	0.8	0.9	0.3	**0.6**	**0.7**	**0.8**	**0.9**
Residential	0.3	0.4	0.3	-0.3	-0.2	0.0	0.3	0.3	**0.1**	**0.2**	**0.2**	**0.3**
Exports	-0.2	1.0	0.5	1.2	-0.8	0.9	0.5	0.4	**0.6**	**0.9**	**0.9**	**0.8**
Imports	-0.1	-1.1	-0.4	-0.2	-0.1	-0.8	-0.4	-0.2	**0.3**	**0.4**	**0.4**	**0.4**
Government	-0.8	-0.1	0.1	-1.0	-0.2	-0.7	-0.2	-0.4	**-0.2**	**0.0**	**0.0**	**0.0**
Unemployment Rate (%, average)	7.7	7.5	7.2	7.0	6.7	8.9	8.1	7.4	**6.6**	**5.9**	**5.6**	**5.2**
Average Monthly Nonfarm Payroll (K)	206	201	172	198	190	174	186	194	**195**	**210**	**231**	**250**
CPI (YoY %)	1.7	1.4	1.5	1.2	1.4	3.1	2.1	1.5	**1.8**	**2.2**	**2.3**	**2.4**
Core CPI (YoY %)	1.9	1.7	1.7	1.7	1.6	1.7	2.1	1.8	**1.9**	**2.1**	**2.3**	**2.4**
Fiscal Balance (% GDP)	-	-	-	-	-	-8.7	-6.8	-4.1	**-3.0**	**-2.7**	**-2.9**	**-3.0**
Current Account (bop, % GDP)	-2.5	-2.3	-2.3	-1.9	-	-3.0	-2.7	-2.3	**-2.1**	**-1.8**	**-1.6**	**-1.2**
Fed Target Rate (%, eop)	0.25	0.25	0.25	0.25	0.25	0.25	0.25	0.25	**0.25**	**0.50**	**1.50**	**2.50**
S&P Case-Shiller Index (YoY %)	9.97	9.98	11.24	11.43	10.32	-4.34	2.82	10.67	**8.78**	**6.20**	**4.62**	**3.78**
10-Yr Treasury (% Yield, eop)	1.96	2.30	2.81	2.90	2.72	1.98	1.72	2.90	**3.41**	**3.80**	**4.10**	**4.34**
U.S. Dollar / Euro (eop)	1.30	1.32	1.34	1.37	1.38	1.32	1.31	1.37	**1.35**	**1.32**	**1.37**	**1.36**
Brent Oil Prices (dpb, average)	112.6	102.7	110.3	109.3	108.2	111.3	111.7	108.7	**112.2**	**117.2**	**120.2**	**124.2**

U.S. Economic Outlook

Monthly Update

June 11, 2014