

Economic Analysis

Retail Sales Slow in June as Autos Disappoint

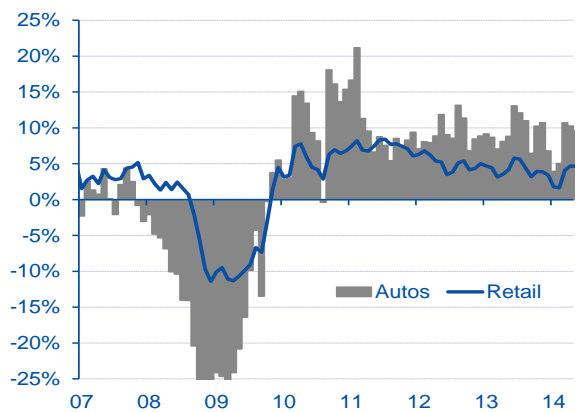
Kim Fraser Chase

Retail sales continued to show modest growth in June, up 0.2% following an upwardly revised 0.5% gain in May. The headline figure was driven by a 1.1% increase in sales at general merchandise stores as well as 0.9% gains from both health and personal care stores and clothing and accessory stores. Sales at gasoline stations increased 0.3%, although this was most likely due to rising price pressures and we expect that the inflation-adjusted data released next week will show a lower monthly change. Surprisingly, auto sales declined 0.3% for the month despite the fact that unit sales have shown significant improvement over the past few months. Excluding autos and gas, retail sales increased 0.4%. Unfortunately, the data do point to some deceleration throughout the past few months, with average monthly growth in 2Q14 slightly lower than that in 1Q14. This is discouraging when it comes to our expectations for the QoQ rebound from the serious first quarter contraction; regardless, personal consumption is likely to remain the strongest driver of GDP growth in the coming quarters.

Industrial Production Not a Shining Star, but Underlying Trends are Positive

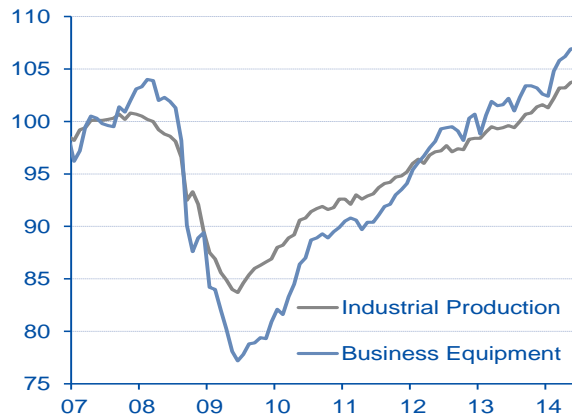
Industrial production was somewhat disappointing in June, rising only 0.2% for the month on the back of a slight downward revision to May's data. As was the case with retail sales, the lower-than-expected growth in June does not present an extremely upbeat picture for the 2Q GDP rebound. Manufacturing output was particularly slow in June, up only 0.1%, despite the fact that various surveys reported significant improvements in the sector's activity for the month. On the bright side, industrial production has remained steady near 4.0% annual growth throughout the past few months and does not show signs of a major downturn in the cycle. In general, industrial production growth at an annualized rate has accelerated from the first quarter at a pace somewhat closer to that seen in 4Q13. When it comes to GDP growth for the second quarter, we have not seen any standout factors that could lead the rebound on its own, but the good news is that we are expecting the subsequent quarters to make up for the losses incurred in 1Q14.

Graph 1
Retail and Auto Sales
YoY % Change



Source: U.S. Census Bureau & BBVA Research

Graph 2
Industrial Production and Business Equipment
SA Index, 2007=100



Source: FRB & BBVA Research

Week Ahead

Consumer Price Index, Core (June, Tuesday 8:30 ET)

Forecast: 0.3%, 0.2%

Consensus: 0.3%, 0.2%

Previous: 0.4%, 0.3%

Inflation has finally begun to show signs of life after igniting deflationary concerns several times throughout the past year. In May, consumer prices shot up 0.4% for the first time since early 2013, while the core index increased at its fastest pace in nearly four years. The latest data hint at another healthy increase in June, with rising oil and natural gas prices expected to drive the headline figure. Excluding food and energy, we should continue to see steady monthly gains in consumer prices, driven primarily by the shelter component.

Existing Home Sales (June, Tuesday 10:00 ET)

Forecast: 4975K

Consensus: 4990K

Previous: 4890K

Existing home sales hit a recovery peak in July 2013 before spiraling downward in the following nine months. May's data signaled the start of an upward trend, jumping almost 5% from April's modest gain. In June, we expect to see another increase in existing home sales, though likely at a slower pace than in the previous month. The significant increase in pending home sales for May suggests that the demand for existing homes has picked back up again after a very slow start to the year.

New Home Sales (June, Thursday 10:00 ET)

Forecast: 525K

Consensus: 476K

Previous: 504K

New home sales are expected to increase in June for the third consecutive month as demand finally breaks away from the relatively flat post-recession trend. Despite the latest disappointing reports for housing starts in May and June, new home construction is still improving on an annual basis. Furthermore, the home builder confidence index jumped back up in June closer to the higher levels seen in December 2013 and January 2014. In particular, the sales component of the housing market index suggests stronger demand for new homes at present and in the next six months. Therefore, we should continue to see gradual improvement in new home sales as the summer gets underway.

Durable Goods Orders (June, Friday 8:30 ET)

Forecast: 1.0%, 0.6%

Consensus: 0.4%, 0.5%

Previous: -0.9%, 0.0%

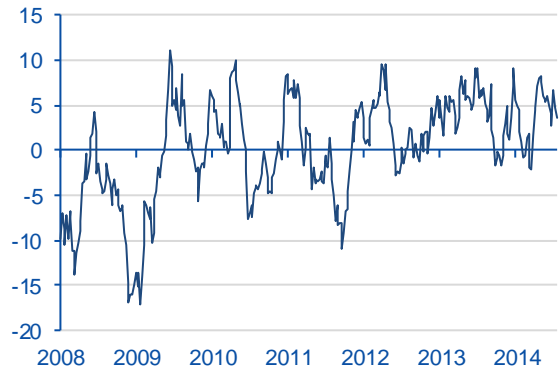
Durable goods new orders have mostly recovered to the pre-crisis peak, although the data continue to show extreme month-to-month volatility. For June, we expect that new orders will increase at both the headline and core levels as the data rebound from weakness seen in May. Recent manufacturing reports for June suggest significant improvement in new orders for June, with the most encouraging data coming from the ISM, Empire State, and Philadelphia Fed manufacturing surveys. A big push in June would certainly help to boost GDP expectations for the quarter.

Market Impact

Markets could remain on edge this week given that there has been a lot of economic information to digest throughout July thus far. Chair Yellen's latest testimony to Congress again puts inflation on a pedestal, and markets will be sensitive to a CPI report that strays even slightly from consensus expectations. Housing data will also be closely watched as the latest reports have been disappointing and are not so encouraging when it comes to the 2Q14 GDP contribution.

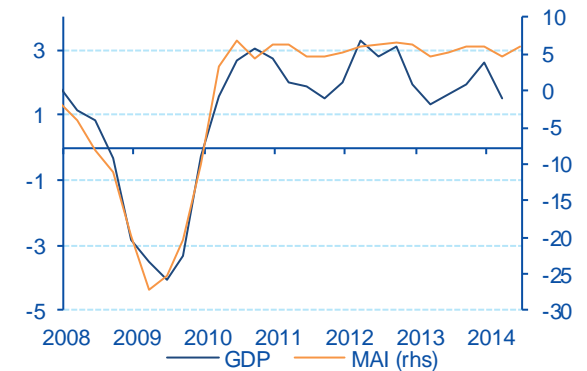
Economic Trends

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



Source: BBVA Research

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



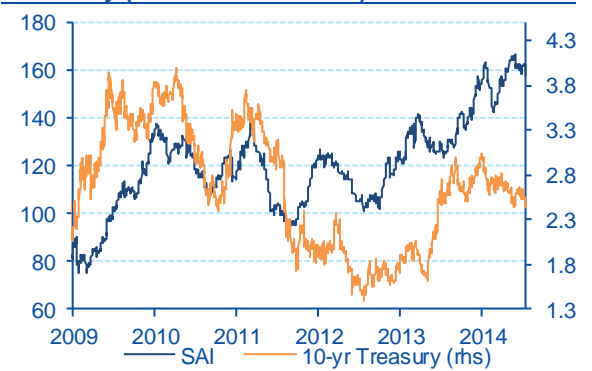
Source: BBVA Research & BEA

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



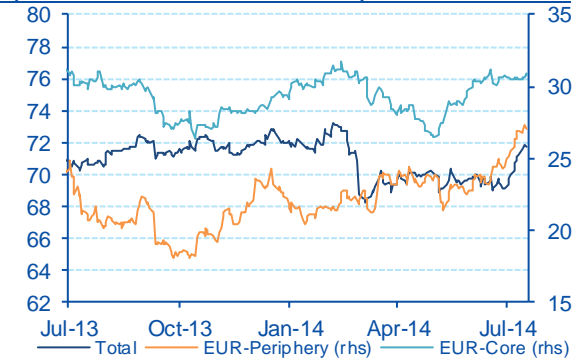
Source: BBVA Research

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



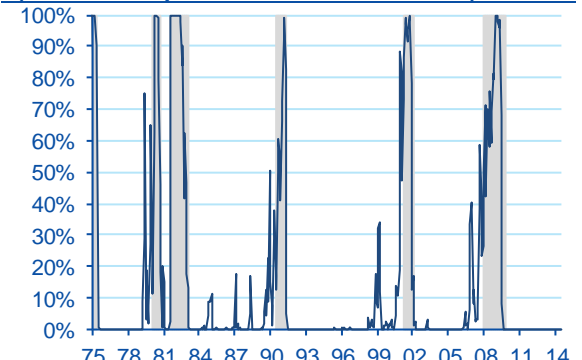
Source: Bloomberg & BBVA Research

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



Source: BBVA Research

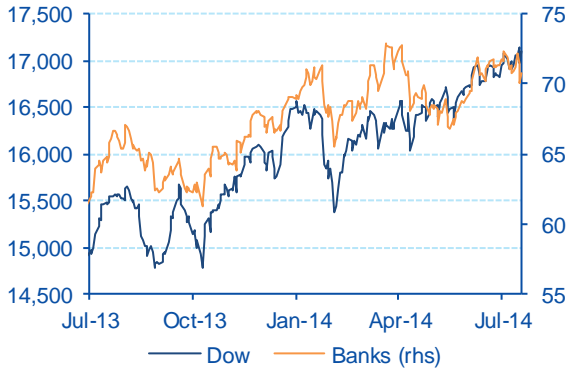
Graph 8
BBVA US Recession Probability Model (Recession episodes in shaded areas, %)



Source: BBVA Research

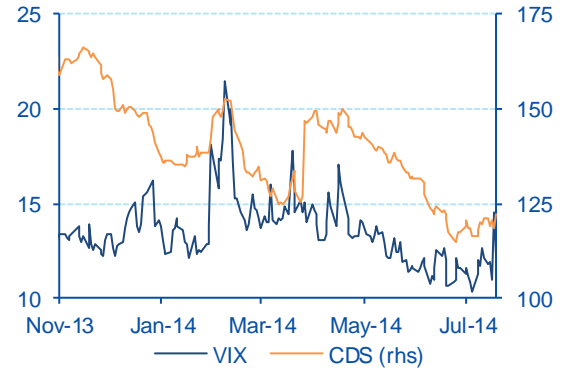
Financial Markets

Graph 9
Stocks
(Index, KBW)



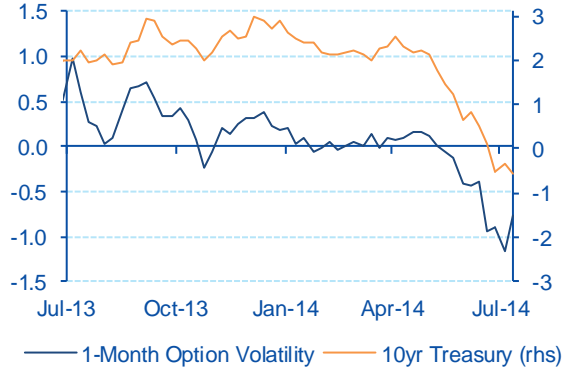
Source: Bloomberg & BBVA Research

Graph 10
Volatility & High-Volatility CDS
(Indices)



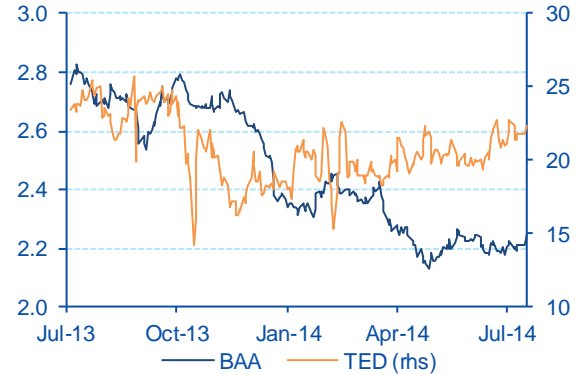
Source: Bloomberg & BBVA Research

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



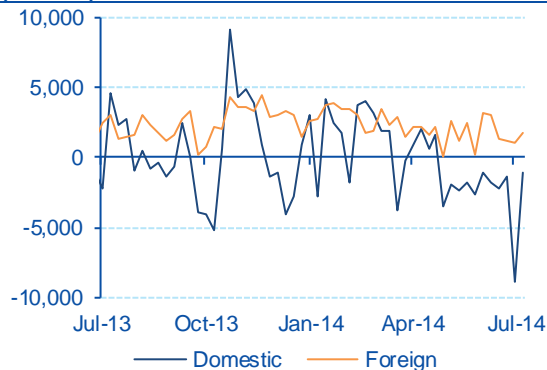
Source: Haver Analytics & BBVA Research

Graph 12
TED & BAA Spreads
(%)



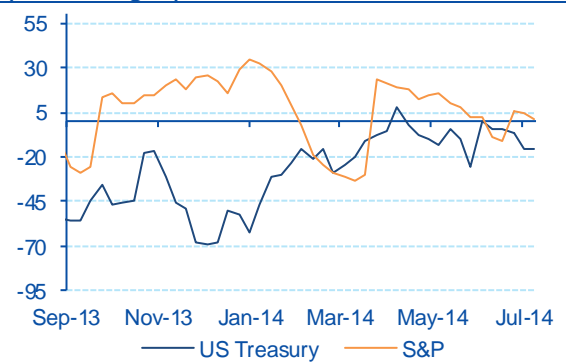
Source: Bloomberg & BBVA Research

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



Source: Haver Analytics & BBVA Research

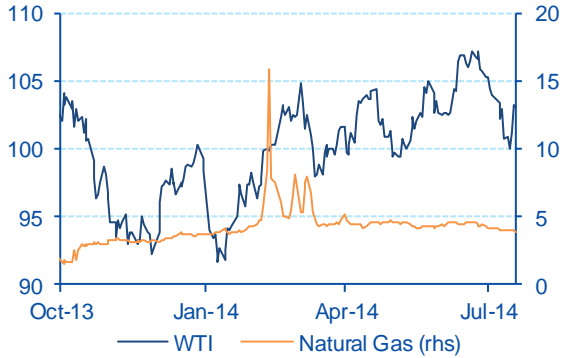
Graph 14
Total Reportable Short & Long Positions
(Short-Long, K)



Source: Haver Analytics & BBVA Research

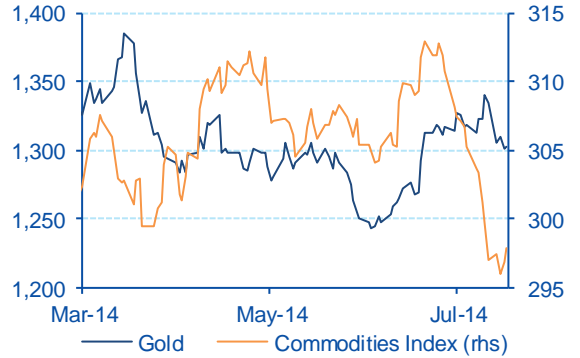
Financial Markets

Graph 15
Commodities
(Dpb & DpMMBtu)



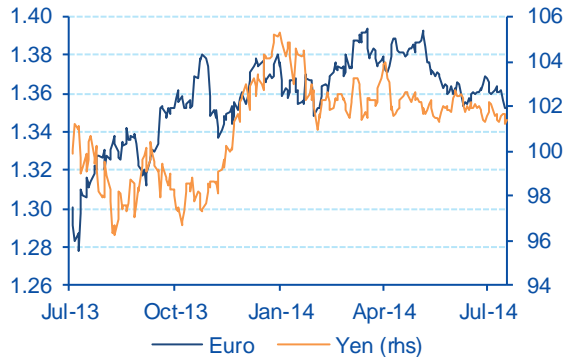
Source: Bloomberg & BBVA Research

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



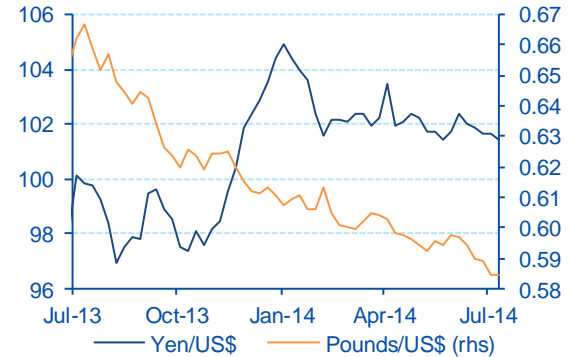
Source: Haver Analytics & BBVA Research

Graph 17
Currencies
(Dpe & Ypd)



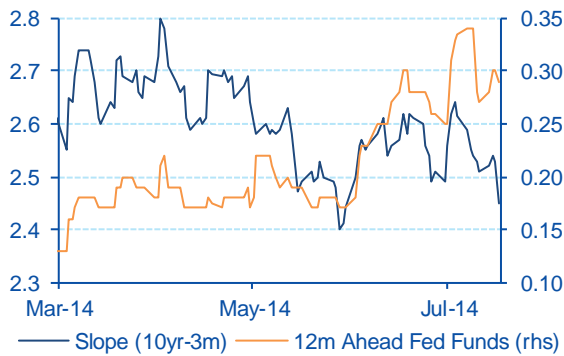
Source: Bloomberg & BBVA Research

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



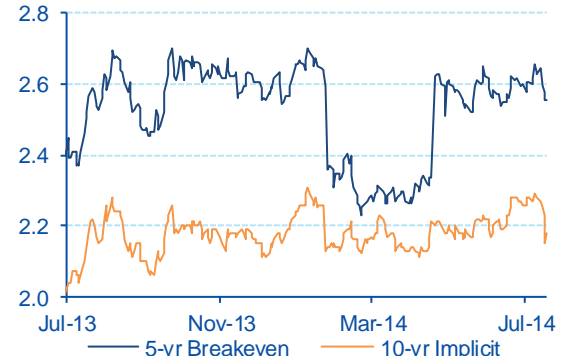
Source: Haver Analytics & BBVA Research

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)	14.86	14.86	14.82	14.10
New Auto (36-months)	2.91	2.90	2.86	2.51
Heloc Loan 30K	4.98	5.00	5.03	5.29
5/1 ARM *	2.97	2.99	3.00	2.90
15-year Fixed Mortgage *	3.23	3.24	3.30	3.23
30-year Fixed Mortgage *	4.13	4.15	4.17	3.99
Money Market	0.41	0.40	0.37	0.44
2-year CD	0.82	0.82	0.81	0.74

*Freddie Mac National Mortgage Homeowner Commitment US
Source: Bloomberg & BBVA Research

Table 2
Key Interest Rates (%)

	Last	Week ago	4-Weeks ago	Year ago
1M Fed	0.09	0.09	0.10	0.09
3M Libor	0.23	0.23	0.23	0.27
6M Libor	0.33	0.33	0.32	0.40
12M Libor	0.55	0.56	0.55	0.68
2yr Sw ap	0.67	0.62	0.61	0.48
5yr Sw ap	1.78	1.74	1.77	1.50
10Yr Sw ap	2.60	2.63	2.70	2.71
30yr Sw ap	3.26	3.30	3.39	3.56
30day CP	0.11	0.12	0.11	0.12
60day CP	0.12	0.11	0.11	0.15
90day CP	0.13	0.13	0.13	0.16

Source: Bloomberg & BBVA Research

Quote of the Week

Janet Yellen, Federal Reserve Board Chair
Semiannual Monetary Policy Report to the Congress
15 July 2014

"It would be a terrible mistake to ask the Federal Reserve to specify a mathematical rule. If we were following a specific mathematical rule, I really think performance in this recovery would have been dreadful."

Economic Calendar

Date	Event	Period	Forecast	Survey	Previous
21-Jul	Chicago Fed National Activity Index	JUN	0.35	0.18	0.21
22-Jul	US CPI Urban Consumers MoM SA	JUN	0.30	0.30	0.35
22-Jul	US CPI Urban Consumers Less Food & Energy MoM SA	JUN	0.20	0.20	0.26
22-Jul	US Existing Homes Sales SAAR	JUN	4.98	4.99	4.89
22-Jul	US Existing Homes Sales MoMSA	JUN	1.74	2.04	4.94
24-Jul	US Initial Jobless Claims SA	JUL 19	300.00	310.00	302.00
24-Jul	US Continuing Jobless Claims SA	JUL 12	2515.00	2512.50	2507.00
24-Jul	US New One Family Houses Sold Annual Total SAAR	JUN	525.00	476.00	504.00
24-Jul	US New One Family Houses Sold Annual Total MoM SA	JUN	4.17	-5.56	18.60
25-Jul	US Durable Goods New Orders Industries MoM SA	JUN	1.00	0.40	-0.90
25-Jul	US Durable Goods New Orders Total ex Transportation MoM SA	JUN	0.60	0.50	0.00

Forecasts (NOTE: revisions pending)

	2011	2012	2013	2014	2015	2016	2017
Real GDP (% SAAR)	1.8	2.8	1.9	2.5	2.5	2.8	2.8
CPI (YoY %)	3.1	2.1	1.5	1.8	2.2	2.3	2.4
CPI Core (YoY %)	1.7	2.1	1.8	1.9	2.1	2.3	2.4
Unemployment Rate (%)	8.9	8.1	7.4	6.6	5.9	5.6	5.2
Fed Target Rate (eop, %)	0.25	0.25	0.25	0.25	0.50	1.50	2.50
10Yr Treasury (eop, % Yield)	1.98	1.72	2.90	3.00	3.50	3.75	4.00
US Dollar/ Euro (eop)	1.31	1.31	1.37	1.31	1.29	1.36	1.36

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