

Economic Analysis

# New Orders Drag Down ISM Manufacturing Index in December

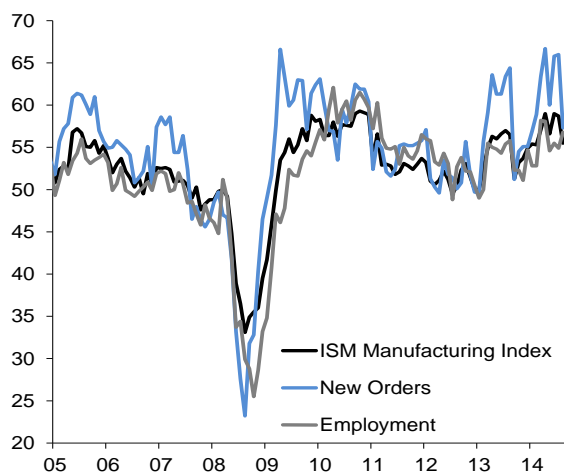
Kim Fraser Chase

The ISM Manufacturing Index declined slightly in December to 55.5, closing out the year in positive territory and above the level seen in January. The index reached a high point for the year back in August and then again in October, but then proceeded to decline in both November and December. Much of this downward pressure was due to minor declines in production and inventories, followed by a significant 13.2% fall in new orders for December. Not surprisingly, the index was also dragged down by a sharp drop in the price index as well as declines in both the import and export components. Looking forward, we expect to see continued forward progress in the manufacturing sector, with activity holding above the 50-mark throughout 2015. This assumes that domestic demand will remain strong and that global demand will not deteriorate further during the year.

## Consumer Confidence Closes out 2014 on a High Note

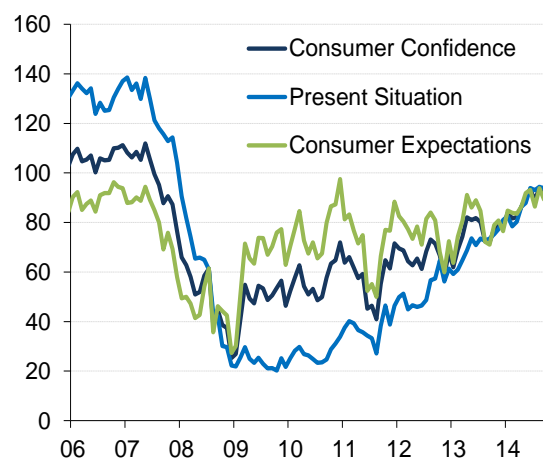
Consumer confidence held near recovery highs in December, rising to 92.6 from 91.0 in November. It is no surprise that confidence was up at the end of the year, with low gas prices continuing to relieve consumers and further lifting holiday spirits. As such, December's report noted a 5.2% monthly gain in views on the present situation to a recovery-high level of 98.6, yet still far off from the pre-recession peak around 138. Consumer expectations, on the other hand, declined for the second consecutive month, most likely reflecting some uncertainty over if and when gas prices will spike back up again. If prices remain low throughout 2015, we should see consumer confidence finally back at pre-recession levels. Although other uncertainties linger, particularly for the global economy, we do not expect this to have much of a direct impact on domestic consumers. Overall, the report highlights the fact that 2014 brought along significant positive changes in the domestic economy, enough to boost consumer confidence more than in previous years.

Graph 1  
**ISM Manufacturing Index (SA, 50+=increasing)**



Source: ISM & BBVA Research

Graph 2  
**Consumer Confidence (SA, 1985=100)**



Source: Conference Board & BBVA Research

## Week Ahead

### ISM Non-Manufacturing Index (December, Tuesday 8:30 ET)

Forecast: 59.7

Consensus: 58.5

Previous: 59.3

The ISM Non-Manufacturing Index is expected to increase slightly in December as domestic demand conditions continue to improve. Services are certainly in full force at the end of the year, when consumers are out shopping and celebrating the holidays. Despite two consecutive declines in September in October, the index remains in expansionary territory and near recovery highs. November's report showed an encouraging pickup in the services sector, particularly in new orders, which indicate upcoming gains in the business activity component.

### International Trade Balance (November, Wednesday 8:30 ET)

Forecast: -\$43.5B

Consensus: -\$42.3B

Previous: -\$43.4B

The international trade balance is not expected to move much in November, holding near a similar level as seen in September and October. Weak global demand continues to put downward pressure on exports, and the volatility in 3Q and 4Q thus far suggest a modest decline for November. However, import growth has been strong as domestic demand picks up for the holiday season. We expect that imports will increase in November for the fifth consecutive month, leading to a slight deterioration in the trade balance but hinting at stronger underlying fundamentals for domestic activity.

### Consumer Credit (November, Thursday 15:00 ET)

Forecast: \$17.1B

Consensus: \$15.3B

Previous: \$13.2B

Consumer credit is expected to increase again in November, continuing the double-digit gains seen throughout the past year. Nonrevolving credit continues to be the primary driver, with student debt and auto loans keeping the figure elevated. The holiday shopping season also brings with it a healthy jump in revolving credit, as consumers become more willing to loosen their purse strings and take on additional credit card debt for big ticket purchases. We will most likely see a slowdown in revolving credit growth after the New Year, although the ongoing trend of low gas prices has boosted consumers' purchasing power and may keep spirits up for increased spending throughout the first part of the year.

### Nonfarm Payrolls and Unemployment Rate (December, Friday 8:30 ET)

Forecast: 220K, 5.8%

Consensus: 250K, 5.7%

Previous: 321K, 5.8%

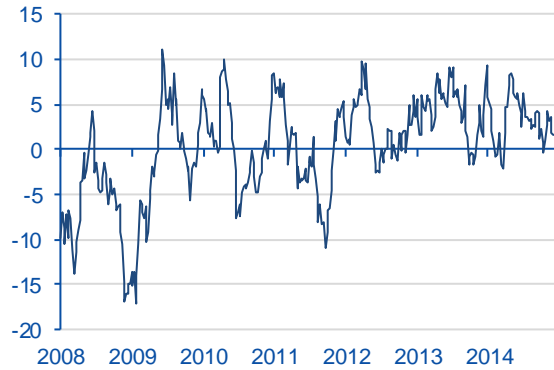
Job growth is expected to continue moving in a positive direction, marking 2014 as the strongest year of the recovery period. In December, we expect nonfarm payrolls to increase at a healthy pace, though slightly less than the drastic 321K jump seen in November. When it comes to the unemployment rate, we expect to see more gradual declines moving into 2015. The falling participation rate played a major role in bringing down the unemployment rate in 2014, but we don't expect to see labor force participation fall much further than its current point near a 35-year low. Still, we expect that the unemployment rate will continue to trend downward, this time influenced by healthier gains in employment.

### Market Impact

The first full week of 2015 starts off strong, with markets patiently awaiting the FOMC minutes and the employment report for December. We expect that markets will be back refreshed and ready to start the New Year, which may itself warrant some reaction as focus returns to global slowdowns and low oil prices.

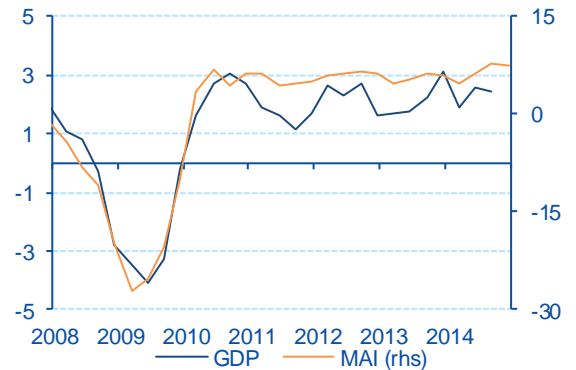
## Economic Trends

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



Source: BBVA Research

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



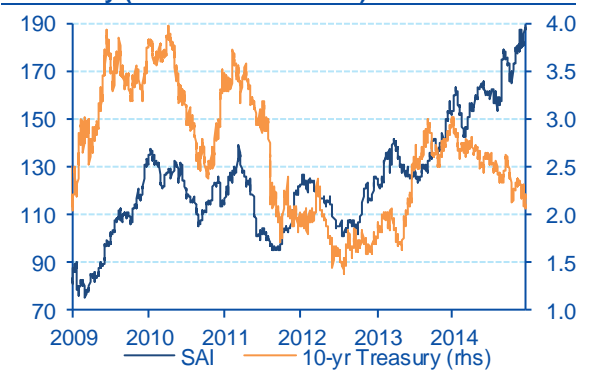
Source: BBVA Research & BEA

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



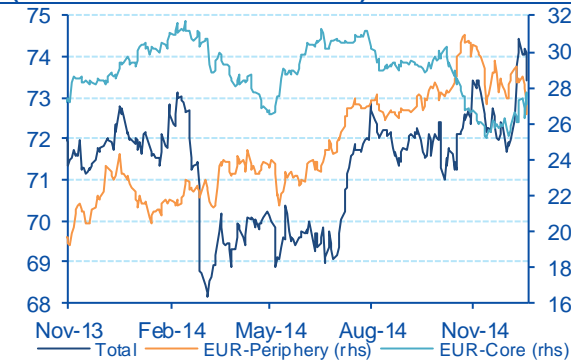
Source: BBVA Research

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



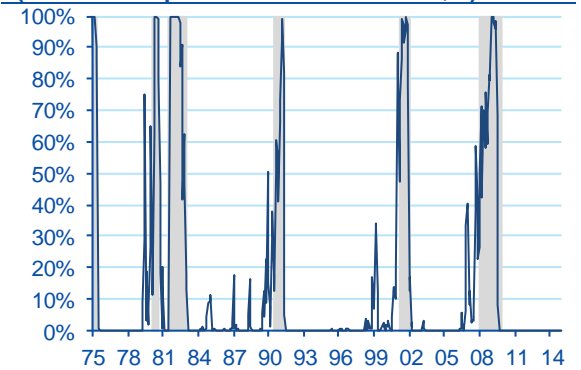
Source: Bloomberg & BBVA Research

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



Source: BBVA Research

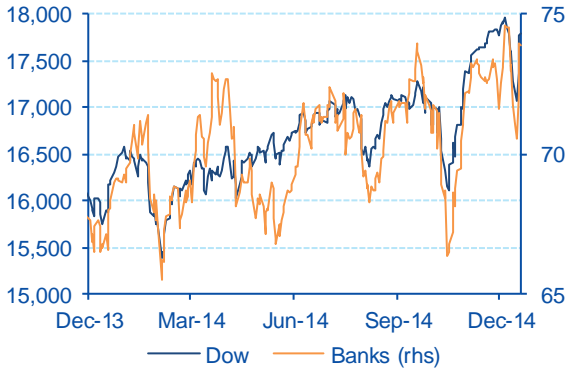
Graph 8  
**BBVA US Recession Probability Model (Recession episodes in shaded areas, %)**



Source: BBVA Research

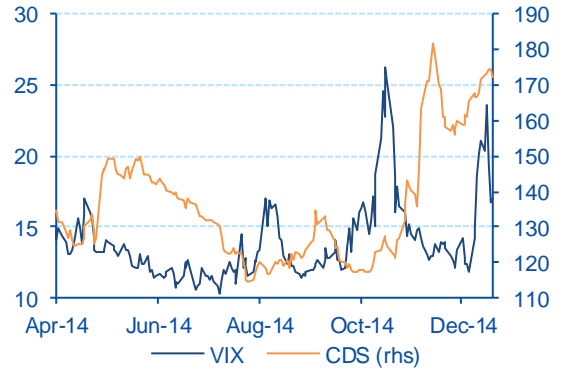
**Financial Markets**

**Graph 9**  
**Stocks**  
**(Index, KBW)**



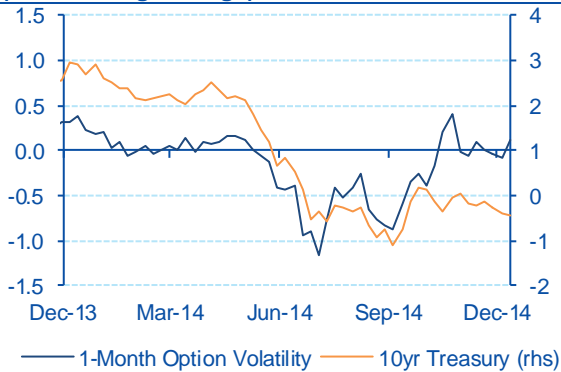
Source: Bloomberg & BBVA Research

**Graph 10**  
**Volatility & High-Volatility CDS**  
**(Indices)**



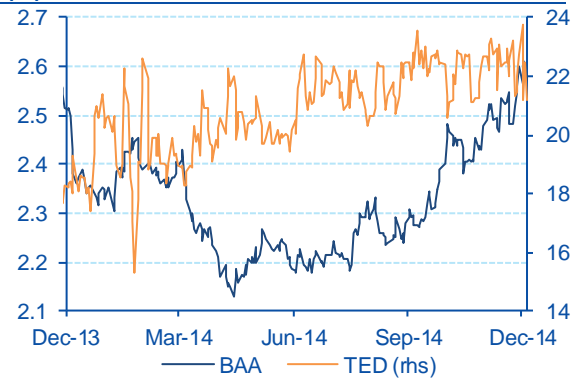
Source: Bloomberg & BBVA Research

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



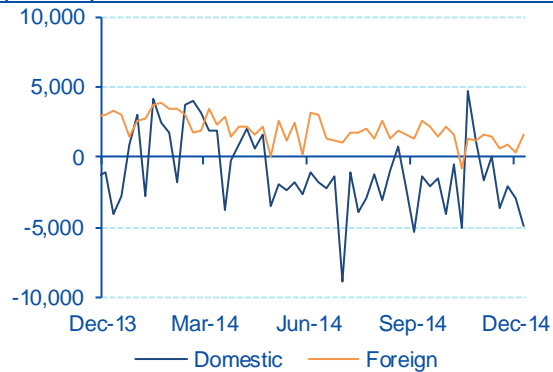
Source: Haver Analytics & BBVA Research

**Graph 12**  
**TED & BAA Spreads**  
**(%)**



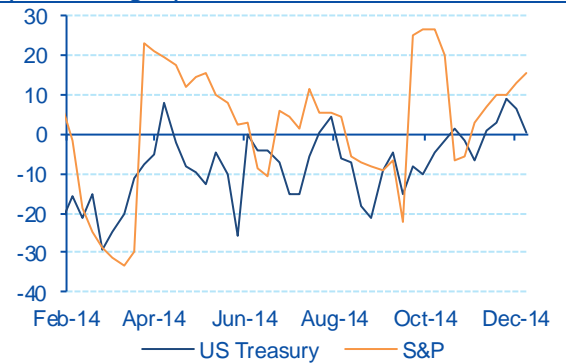
Source: Bloomberg & BBVA Research

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



Source: Haver Analytics & BBVA Research

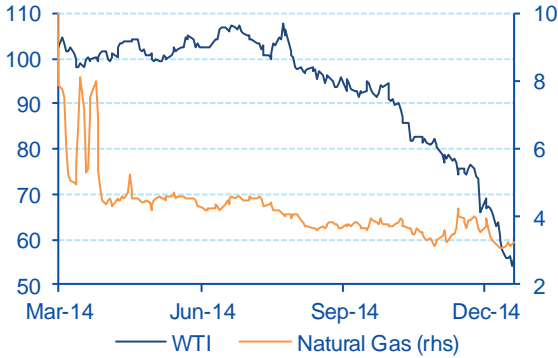
**Graph 14**  
**Total Reportable Short & Long Positions**  
**(Short-Long, K)**



Source: Haver Analytics & BBVA Research

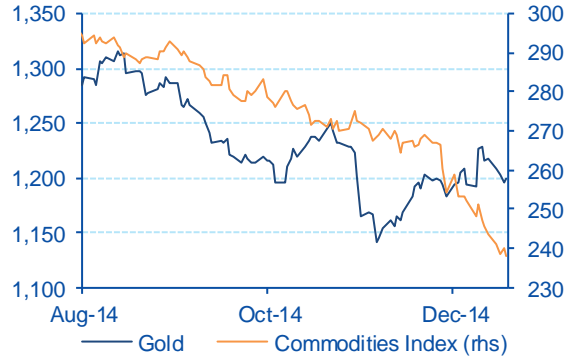
**Financial Markets**

Graph 15  
**Commodities (Dpb & DpMMBtu)**



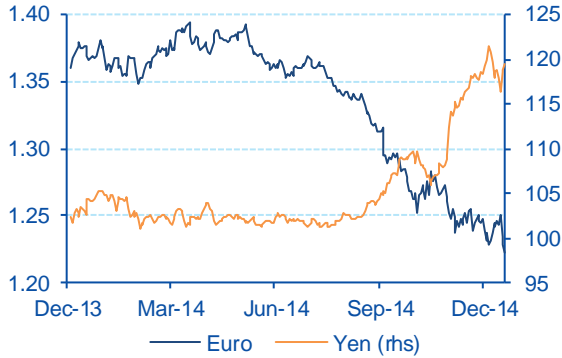
Source: Bloomberg & BBVA Research

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



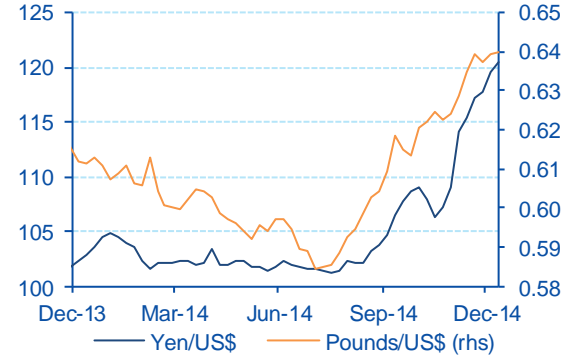
Source: Haver Analytics & BBVA Research

Graph 17  
**Currencies (Dpe & Ypd)**



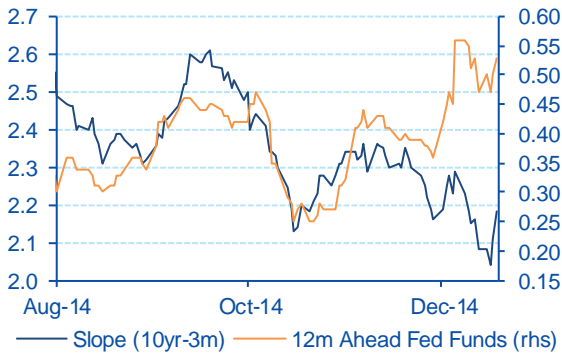
Source: Bloomberg & BBVA Research

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



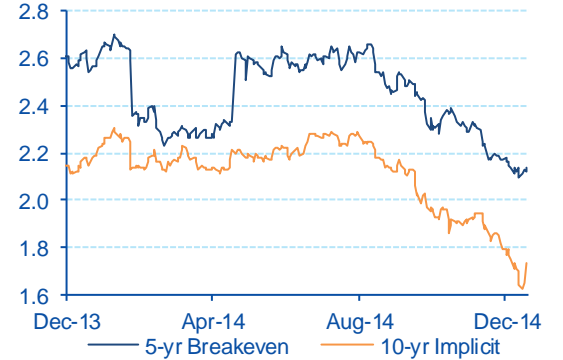
Source: Haver Analytics & BBVA Research

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	14.86	14.10
New Auto (36-months)	2.70	2.84	2.94	2.67
Heloc Loan 30K	4.93	4.91	4.82	5.32
5/1 ARM *	2.95	2.98	3.01	2.90
15-year Fixed Mortgage *	3.09	3.20	3.17	3.23
30-year Fixed Mortgage *	3.80	3.93	3.99	3.99
Money Market	0.43	0.43	0.43	0.42
2-year CD	0.87	0.87	0.87	0.81

\*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	0.13	0.12	0.10	0.09
3M Libor	0.25	0.24	0.23	0.25
6M Libor	0.34	0.34	0.32	0.35
12M Libor	0.61	0.60	0.55	0.58
2yr Sw ap	0.87	0.78	0.72	0.49
5yr Sw ap	1.79	1.66	1.74	1.74
10Yr Sw ap	2.31	2.21	2.43	3.05
30yr Sw ap	2.74	2.70	2.99	3.86
30day CP	0.12	0.12	0.11	0.12
60day CP	0.13	0.11	0.11	0.15
90day CP	0.15	0.13	0.13	0.14

Source: Bloomberg & BBVA Research

## Quote of the Week

President Barack Obama

Remarks by the President in Year-End Press Conference

19 December 2014

*"In last year's final press conference, I said that 2014 would be a year of action and would be a breakthrough year for America. And it has been. Yes, there were crises that we had to tackle around the world, many that were unanticipated. We have more work to do to make sure our economy, our justice system, and our government work not just for the few, but for the many. But there is no doubt that we can enter into the New Year with renewed confidence that America is making significant strides where it counts."*

## Economic Calendar

Date	Event	Period	Forecast	Survey	Previous
5-Jan	Motor Vehicle Sales	DEC	17.10	17.00	17.20
6-Jan	Factory Orders MoM %	NOV	-0.30	-0.20	-0.70
6-Jan	ISM Non Manufacturing Index	DEC	59.70	58.50	59.30
7-Jan	ADP Employment MoM	DEC	215.00	238.00	208.00
7-Jan	International Trade Balance	NOV	-43.50	-42.30	-43.40
8-Jan	Initial Jobless Claims	3-Jan	295.00	290.00	298.00
8-Jan	Continuing Claims	27-Dec	2375.00	2360.00	2353.00
8-Jan	Consumer Credit MoM	NOV	17.10	15.30	13.20
9-Jan	Nonfarm Payrolls MoM	DEC	220.00	250.00	321.00
9-Jan	Private Payrolls MoM	DEC	217.00	250.00	314.00
9-Jan	Manufacturing Payrolls MoM	DEC	10.00	15.00	28.00
9-Jan	Unemployment Rate	DEC	5.80	5.70	5.80
9-Jan	Wholesale Inventories MoM %	NOV	0.40	0.40	0.40

## Forecasts

	2011	2012	2013	2014	2015	2016	2017
Real GDP (% SAAR)	1.8	2.8	1.9	2.0	2.5	2.8	2.8
CPI (YoY %)	3.1	2.1	1.5	1.7	2.0	2.1	2.4
CPI Core (YoY %)	1.7	2.1	1.8	1.8	2.1	2.2	2.4
Unemployment Rate (%)	8.9	8.1	7.4	6.2	5.8	5.5	5.0
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	2.30	3.12	3.67	3.90
US Dollar/ Euro (eop)	1.31	1.31	1.37	1.23	1.20	1.24	1.28

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