

# Economic Watch

US

Houston, April 7, 2014  
Economic Analysis

## Monthly US Outlook: April A Late Spring for Economic Activity

US

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- Soft start to 2014 but the winter weather impact is slowly subsiding
- Low inflation only temporary but possibly more influential for Fed action
- GDP forecast stands at 2.5% for 2014, with balanced risks to growth

A prolonged winter has certainly had its impact on economic activity, keeping consumers indoors and hitting manufacturing and construction particularly hard. While it doesn't quite feel like spring has truly arrived, we are at least starting to see signs of improvement in economic data. We do expect to see a softer pace of growth in 1Q14 after a strong 2H13, but our short-term models suggest a pickup in momentum throughout the spring and summer months, driven in large part by a recovery in the aforementioned sectors as well as an overall confidence boost among businesses and consumers.

The employment situation is gaining traction once again, with nonfarm payroll growth just barely missing the 200K mark in March as more people re-entered the workforce. Although the unemployment rate declined much faster-than-expected throughout 2013 (from 7.9% in January to 6.7% in December), we expect that modest improvement in labor force participation will prevent such a rapid drop in 2014. In fact, we expect that the unemployment rate will remain above 6.0% throughout the rest of this year and into 2015, with employment growth averaging just below 200K per month. At the same time, significant resource slack will keep downward pressure on wage growth for the foreseeable future.

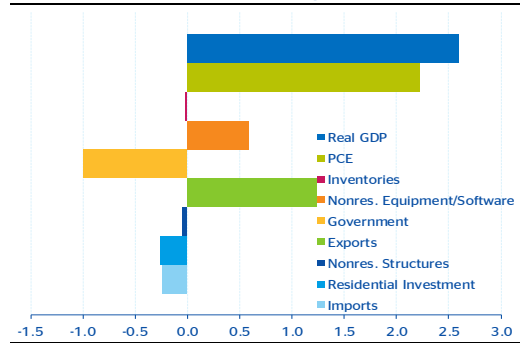
Lately it has become clearer that economic expansion is not translating into higher inflation, though this is not a new phenomenon. Even still, the risk of deflation in the U.S. is very low. Our short-term forecasts suggest that moderate inflationary pressures in 2014 will arise from medical care, shelter, and energy, while food prices will likely remain subdued. Over the longer term, inflation is likely to remain lower than average ([see our latest brief on inflation](#)).

With ongoing developments related to employment and inflation, the Federal Reserve has its hands full. While there are certainly positive signs coming from the labor market, long-term unemployment conditions remain weak. Accordingly, the Fed decided to step back from its 6.5% unemployment rate threshold while maintaining the 2.0% inflation target. If inflation does not increase even modestly in the short-term, the Fed may be inclined to prolong the QE3 tapering process. However, we continue to expect an end to tapering in 4Q14, with the first fed funds rate hike in mid-2015. In the most recent FOMC meeting, the Committee reaffirmed their strategy to keep interest rates low, carefully balancing the expected timelines for tapering and policy normalization ([see our latest FedWatch](#)).

Despite some short-term drawbacks to growth that developed from the polar vortex hitting most of the U.S., risks remain relatively balanced. On the downside, lack of improvement in the labor market and slowing demand from abroad remain on our radar. Similarly, we could see inflation remain low for a prolonged period of time, igniting further action from the Fed as the economy goes down an uneven and unsustainable road to expansion. However, upside risk could stem from a number of possibilities, including a more immediate rise in inflation to the Fed's 2.0% target as well as a global boost in economic confidence. Overall, we continue to expect that growth will accelerate in 2014, with real GDP growth expected to hit 2.5% for the year.

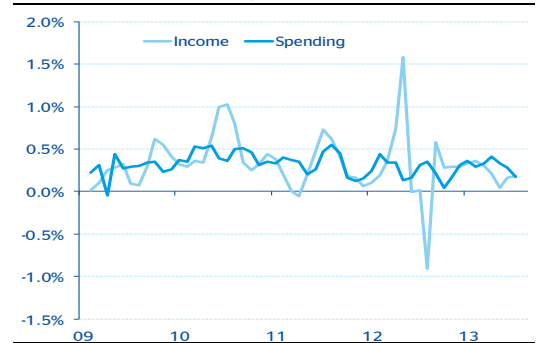
### Economic Indicators

**Graph 1**  
Contributions to Real GDP Growth  
(4Q13 Final, SAAR Percentage Points)



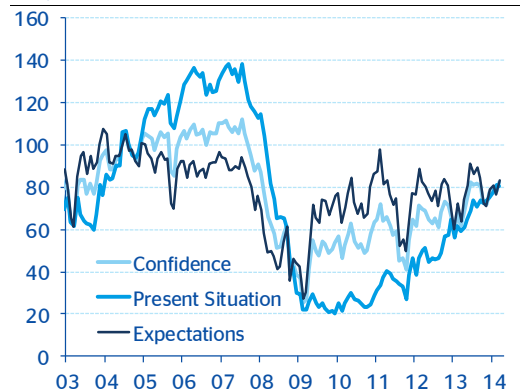
Source: BEA and BBVA Research

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



Source: BEA and BBVA Research

**Graph 3**  
Consumer Confidence  
(SA, Index 1985=100)



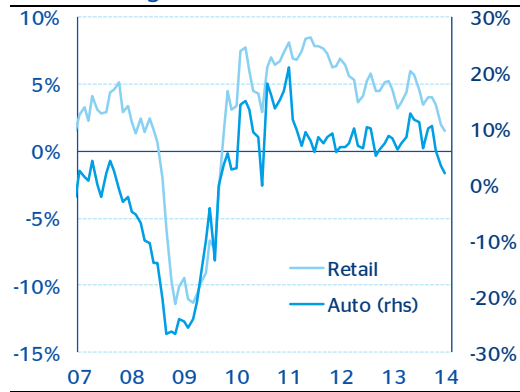
Source: Conference Board and BBVA Research

**Graph 4**  
ISM Indices  
(SA, 50+ = Expansion)



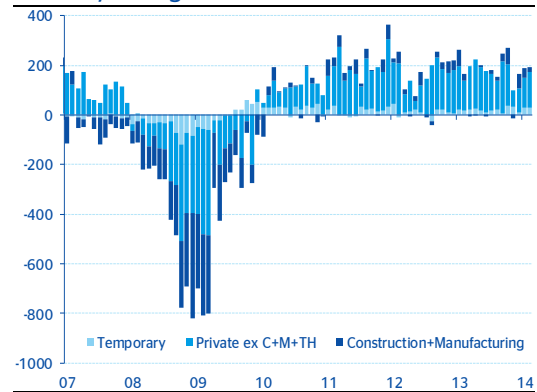
Source: ISM and BBVA Research

**Graph 5**  
Retail and Auto Sales  
(YoY % Change)



Source: US Census Bureau and BBVA Research

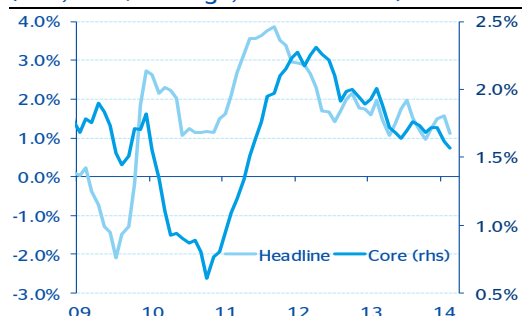
**Graph 6**  
Private Nonfarm Payrolls  
(Monthly Change in K)



Source: BLS and BBVA Research

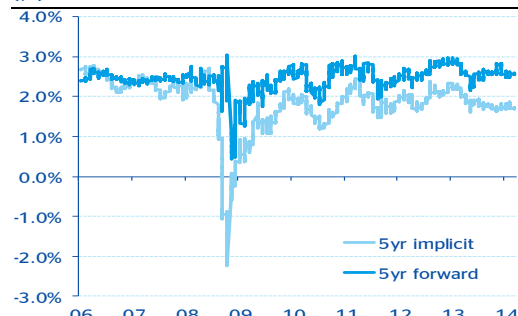
### Economic Indicators

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



Source: BLS and BBVA Research

Graph 8  
Inflation Expectations  
(%)



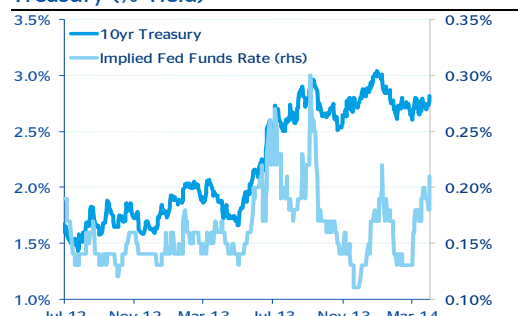
Source: Federal Reserve Board and BBVA Research

Graph 9  
New and Existing Home Sales  
(Thousands)



Source: US Census Bureau, NAR, and BBVA Research

Graph 10  
12-Month Implied Fed Funds Rate & 10-Yr Treasury  
(% Yield)



Source: Federal Reserve Board and BBVA Research

Table 1  
Forecasts (BOLD=FORECASTS) [NOTE: FORECAST REVISIONS PENDING]

	1Q13	2Q13	3Q13	4Q13	1Q14	2011	2012	2013	2014	2015	2016	2017
Real GDP (% SAAR)	1.1	2.5	4.1	2.6	<b>1.6</b>	1.8	2.8	1.9	<b>2.5</b>	<b>2.5</b>	<b>2.8</b>	<b>2.8</b>
Real GDP (Contribution, pp)												
PCE	1.5	1.2	1.4	2.2	<b>0.8</b>	1.7	1.5	1.4	<b>1.3</b>	<b>1.2</b>	<b>1.3</b>	<b>1.2</b>
Gross Investment	0.7	1.4	2.6	0.4	<b>0.2</b>	0.7	1.4	0.8	<b>0.9</b>	<b>0.9</b>	<b>1.0</b>	<b>1.1</b>
Non Residential	-0.6	0.6	0.6	0.7	<b>0.6</b>	0.8	0.9	0.3	<b>0.7</b>	<b>0.9</b>	<b>0.9</b>	<b>0.9</b>
Residential	0.3	0.4	0.3	-0.3	<b>0.2</b>	0.0	0.3	0.3	<b>0.2</b>	<b>0.3</b>	<b>0.3</b>	<b>0.3</b>
Exports	-0.2	1.0	0.5	1.2	<b>0.7</b>	0.9	0.5	0.4	<b>0.8</b>	<b>1.0</b>	<b>0.8</b>	<b>0.8</b>
Imports	-0.1	-1.1	-0.4	-0.2	<b>0.6</b>	-0.8	-0.4	-0.2	<b>0.5</b>	<b>0.5</b>	<b>0.3</b>	<b>0.4</b>
Government	-0.8	-0.1	0.1	-1.0	<b>0.0</b>	-0.7	-0.2	-0.4	<b>-0.2</b>	<b>0.0</b>	<b>0.0</b>	<b>0.0</b>
Unemployment Rate (% average)	7.7	7.5	7.2	7.0	6.7	8.9	8.1	7.4	<b>6.7</b>	<b>6.2</b>	<b>5.7</b>	<b>5.2</b>
Average Monthly Nonfarm Payroll (K)	206	201	172	198	178	174	186	194	<b>196</b>	<b>226</b>	<b>245</b>	<b>273</b>
CPI (YoY %)	1.7	1.4	1.5	1.2	<b>1.4</b>	3.1	2.1	1.5	<b>2.3</b>	<b>2.4</b>	<b>2.4</b>	<b>2.5</b>
Core CPI (YoY %)	1.9	1.7	1.7	1.7	<b>1.7</b>	1.7	2.1	1.8	<b>2.0</b>	<b>2.3</b>	<b>2.4</b>	<b>2.5</b>
Fiscal Balance (% GDP)	-	-	-	-	-	-8.7	-6.8	-4.2	<b>-3.1</b>	<b>-2.7</b>	<b>-2.9</b>	<b>-3.0</b>
Current Account (bop, % GDP)	-2.5	-2.3	-2.3	-	-	-3.0	-2.7	-2.3	<b>-2.6</b>	<b>-2.2</b>	<b>-2.0</b>	<b>-1.4</b>
Fed Target Rate (% eop)	0.25	0.25	0.25	0.25	0.25	0.25	0.25	0.25	<b>0.25</b>	<b>0.50</b>	<b>1.50</b>	<b>2.50</b>
S&P Case-Shiller Index (YoY %)	9.93	9.96	11.15	11.30	<b>9.68</b>	-4.35	2.85	10.60	<b>8.78</b>	<b>6.20</b>	<b>4.62</b>	<b>3.78</b>
10-Yr Treasury (% Yield, eop)	1.96	2.30	2.81	2.90	2.72	1.98	1.72	2.90	<b>3.41</b>	<b>3.80</b>	<b>4.10</b>	<b>4.34</b>
U.S. Dollar / Euro (eop)	1.30	1.32	1.34	1.37	1.38	1.32	1.31	1.37	<b>1.35</b>	<b>1.32</b>	<b>1.37</b>	<b>1.36</b>
Brent Oil Prices (dps, average)	112.6	102.7	110.3	109.3	108.2	111.3	111.7	108.7	<b>112.5</b>	<b>117.2</b>	<b>120.2</b>	<b>124.2</b>

Source: BBVA Research

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