

Economic Watch

US

Houston, March 23rd, 2011
Economic Analysis

US

Principal Economist
Ignacio San Martín
Ignacio.sanmartin@bbva.compass.com
1 713 881 0620

Residential investment will recover in the second half of 2011

- **The latest residential real estate data is raising questions about the strength of economic recovery**

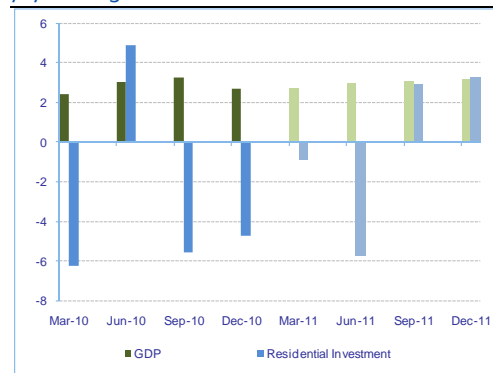
Declining housing prices, weak sales and poor housing starts are increasing the probability of an economic double dip. However, a detailed analysis of the data shows that both the residential market and residential investment should recover in the second half of 2011, in line with our forecasts (chart 1).

- **Foreclosures are moving existing home sales**

In 2010 and the first months of 2011, home sales have been affected by foreclosures and bank short-selling. Although in late 2010 existing home sales increased significantly, in the first months of 2011 data show a downwards trend, which can also be seen in the number of foreclosures and the residential properties owned by the commercial banks (chart 2). The descending trend in new residential delinquency and the improved quality of the residential mortgage portfolio suggest that a slow reduction in the number of forecloses and short sales would lead to a lower supply of this type of dwellings during 2011.

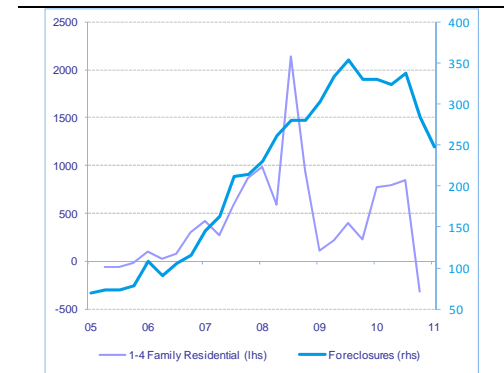
Declining housing auctions would lead to a 2% reduction in sales of existing homes, to around 4.18 million single family units at the end of 2011. However, the market for new homes will benefit and sales could rise by an average of 15% over the year. This surge in sales will lead to increased construction activity given the low level of new housing for sale. This increase in new housing demand will result in positive growth rates of residential investment in the second half of 2011.

Chart 1
GDP and Residential Investment
yoy % change



Source: BEA and BBVA Research

Chart 2
Other Real Estate Owned & Residential Foreclosures
Quarterly variation (\$Mn) and number of filings (MA3M 000's)



Source: FDIC, RealtyTrac and BBVA Research

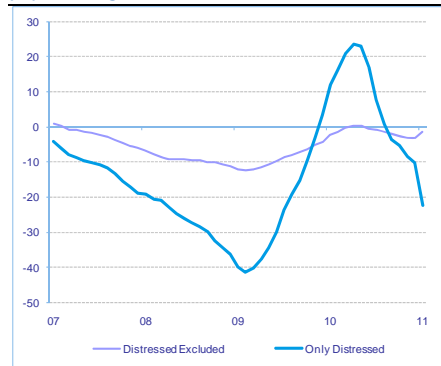
- **Housing prices of non distressed properties are stabilizing**

The trend as regards housing prices has also been affected by foreclosures and short sales since the beginning of the housing meltdown. Indeed, the house price index that excludes distressed homes shows a less volatile and more stable trend than the distressed properties index (chart 3). Since the peak prices in early 2006 to the end of 2010, the distressed properties price index has fallen by almost 60%; the index which excludes foreclosures have fallen 22%. Throughout 2011 housing prices will tend to stabilize as the weight of auctioned homes falls and the importance of the structural factors in demand formation increases. The increase in the number of households, the positive growth of family income and the low mortgage rates will all contribute to price stability.

- **Deleveraging will limit housing demand**

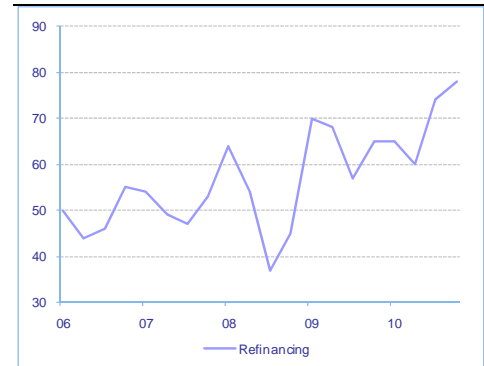
However, there are two elements that will limit the expansion of housing demand in 2011: the high credit standards still maintained by the credit institutions and the mortgage deleveraging that began in mid-2008. Deleveraging will not end until mid-2012, according to our forecasts. Thus, in 2010 mortgages originations were aimed more at refinancing than at purchasing homes; in fact, at the end of the year refinancing accounted for 78% of the total, 13 basis points above the weight it had at the end of 2009 (chart 4).

Chart 3
Housing Price Index
yoy % change



Source: Core Logic and BBVA Research

Chart 4
Mortgage Origination. 1-4 Family
Refinance share (%)



Source: Mortgage Bankers Association

DISCLAIMER

This document and the information, opinions, estimates and recommendations expressed herein, have been prepared by Banco Bilbao Vizcaya Argentaria, S.A. (hereinafter called "BBVA") to provide its customers with general information regarding the date of issue of the report and are subject to changes without prior notice. BBVA is not liable for giving notice of such changes or for updating the contents hereof.

This document and its contents do not constitute an offer, invitation or solicitation to purchase or subscribe to any securities or other instruments, or to undertake or divest investments. Neither shall this document nor its contents form the basis of any contract, commitment or decision of any kind.

Investors who have access to this document should be aware that the securities, instruments or investments to which it refers may not be appropriate for them due to their specific investment goals, financial positions or risk profiles, as these have not been taken into account to prepare this report. Therefore, investors should make their own investment decisions considering the said circumstances and obtaining such specialized advice as may be necessary. The contents of this document is based upon information available to the public that has been obtained from sources considered to be reliable. However, such information has not been independently verified by BBVA and therefore no warranty, either express or implicit, is given regarding its accuracy, integrity or correctness. BBVA accepts no liability of any type for any direct or indirect losses arising from the use of the document or its contents. Investors should note that the past performance of securities or instruments or the historical results of investments do not guarantee future performance.

The market prices of securities or instruments or the results of investments could fluctuate against the interests of investors. Investors should be aware that they could even face a loss of their investment. Transactions in futures, options and securities or high-yield securities can involve high risks and are not appropriate for every investor. Indeed, in the case of some investments, the potential losses may exceed the amount of initial investment and, in such circumstances, investors may be required to pay more money to support those losses. Thus, before undertaking any transaction with these instruments, investors should be aware of their operation, as well as the rights, liabilities and risks implied by the same and the underlying stocks. Investors should also be aware that secondary markets for the said instruments may be limited or even not exist.

BBVA or any of its affiliates, as well as their respective executives and employees, may have a position in any of the securities or instruments referred to, directly or indirectly, in this document, or in any other related thereto; they may trade for their own account or for third-party account in those securities, provide consulting or other services to the issuer of the aforementioned securities or instruments or to companies related thereto or to their shareholders, executives or employees, or may have interests or perform transactions in those securities or instruments or related investments before or after the publication of this report, to the extent permitted by the applicable law.

BBVA or any of its affiliates' salespeople, traders, and other professionals may provide oral or written market commentary or trading strategies to its clients that reflect opinions that are contrary to the opinions expressed herein. Furthermore, BBVA or any of its affiliates' proprietary trading and investing businesses may make investment decisions that are inconsistent with the recommendations expressed herein. No part of this document may be (i) copied, photocopied or duplicated by any other form or means (ii) redistributed or (iii) quoted, without the prior written consent of BBVA. No part of this report may be copied, conveyed, distributed or furnished to any person or entity in any country (or persons or entities in the same) in which its distribution is prohibited by law. Failure to comply with these restrictions may breach the laws of the relevant jurisdiction.

In the United Kingdom, this document is directed only at persons who (i) have professional experience in matters relating to investments falling within article 19(5) of the financial services and markets act 2000 (financial promotion) order 2005 (as amended, the "financial promotion order"), (ii) are persons falling within article 49(2) (a) to (d) ("high net worth companies, unincorporated associations, etc.") Of the financial promotion order, or (iii) are persons to whom an invitation or inducement to engage in investment activity (within the meaning of section 21 of the financial services and markets act 2000) may otherwise lawfully be communicated (all such persons together being referred to as "relevant persons"). This document is directed only at relevant persons and must not be acted on or relied on by persons who are not relevant persons. Any investment or investment activity to which this document relates is available only to relevant persons and will be engaged in only with relevant persons. The remuneration system concerning the analyst/s author/s of this report is based on multiple criteria, including the revenues obtained by BBVA and, indirectly, the results of BBVA Group in the fiscal year, which, in turn, include the results generated by the investment banking business; nevertheless, they do not receive any remuneration based on revenues from any specific transaction in investment banking.

BBVA is not a member of the FINRA and is not subject to the rules of disclosure affecting such members.

"BBVA is subject to the BBVA Group Code of Conduct for Security Market Operations which, among other regulations, includes rules to prevent and avoid conflicts of interests with the ratings given, including information barriers. The BBVA Group Code of Conduct for Security Market Operations is available for reference at the following web site: www.bbva.com / Corporate Governance".

BBVA is a bank supervised by the Bank of Spain and by Spain's Stock Exchange Commission (CNMV), registered with the Bank of Spain with number 0182.