

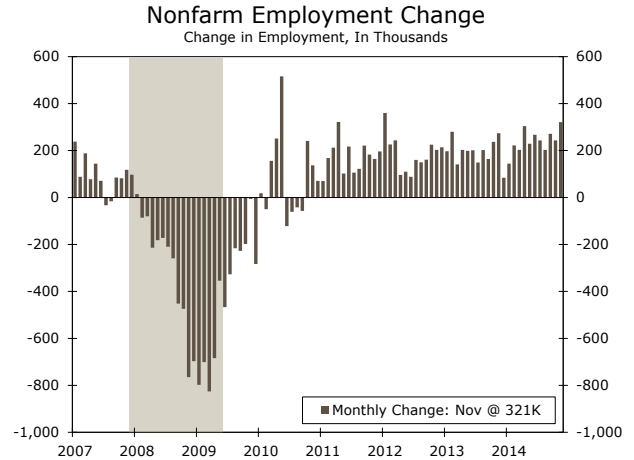
Economics Group

Weekly Economic & Financial Commentary

U.S. Review

Blockbuster Payrolls Set the Tone

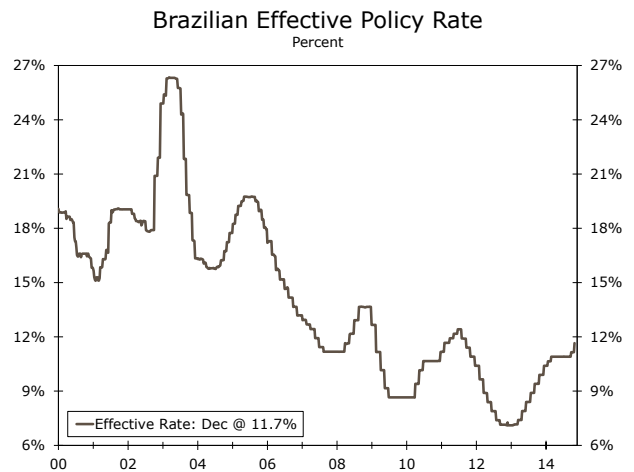
- Nonfarm payrolls surged 321,000 in November, as the workweek and average hourly earnings picked up. The employment report, coupled with lower gas prices, bodes well for consumption in the fourth quarter.
- The ISM manufacturing and non-manufacturing indices remained firmly in expansion territory, with solid gains in the new orders and export orders components.
- The U.S. trade deficit narrowed slightly in October, as export growth outpaced imports, though this comes after a sizable widening of the deficit in the previous month.



Global Review

Brazilian Central Bank Pushes Forward

- The Brazilian central bank surprised markets in late October, just days after the second round of presidential elections, when it raised the Selic benchmark interest rate by 25 bps. The central bank sent an even stronger signal to markets on Dec 3, pushing the Selic rate 50 bps higher to take it to 11.75 percent, in an attempt to keep a lid on the Brazilian currency and inflation expectations.
- The current shift in policy direction from what President Rousseff followed during her first term in office could be signaling a larger influence by ex-President Da Silva in the Rousseff administration.



Wells Fargo U.S. Economic Forecast													
	Actual				Forecast				Actual		Forecast		
	2014				2015				2012	2013	2014	2015	2016
	1Q	2Q	3Q	4Q	1Q	2Q	3Q	4Q					
Real Gross Domestic Product ¹	-2.1	4.6	3.9	1.3	2.7	2.4	2.7	2.9	2.3	2.2	2.2	2.7	2.9
Personal Consumption	1.2	2.5	2.2	2.8	2.5	2.6	2.5	2.6	1.8	2.4	2.3	2.6	2.6
Inflation Indicators ²													
PCE Deflator	1.1	1.6	1.5	1.4	1.5	1.4	1.6	1.9	1.8	1.2	1.4	1.6	2.0
Consumer Price Index	1.4	2.1	1.8	1.6	1.6	1.4	1.7	2.2	2.1	1.5	1.7	1.7	2.4
Industrial Production ¹	3.9	5.7	3.3	3.4	5.0	4.9	4.9	4.9	3.8	2.9	4.0	4.5	4.2
Corporate Profits Before Taxes ²	-4.8	0.1	0.4	4.0	4.1	4.2	4.4	4.5	11.4	4.2	0.0	4.3	3.4
Trade Weighted Dollar Index ³	76.9	75.9	81.3	82.5	83.0	83.8	84.5	85.5	73.5	75.9	79.1	84.2	87.2
Unemployment Rate	6.7	6.2	6.1	5.8	5.7	5.6	5.5	5.4	8.1	7.4	6.2	5.6	5.2
Housing Starts ⁴	0.93	0.99	1.03	1.00	1.06	1.13	1.21	1.24	0.78	0.92	1.01	1.16	1.26
Quarter-End Interest Rates ⁵													
Federal Funds Target Rate	0.25	0.25	0.25	0.25	0.25	0.50	0.75	1.00	0.25	0.25	0.25	0.63	2.00
Conventional Mortgage Rate	4.34	4.16	4.16	4.26	4.31	4.44	4.46	4.62	3.66	3.98	4.23	4.46	5.32
10 Year Note	2.73	2.53	2.52	2.45	2.50	2.71	2.79	2.86	1.80	2.35	2.56	2.71	3.40

Forecast as of: November 26, 2014

¹ Compound Annual Growth Rate Quarter-over-Quarter

² Year-over-Year Percentage Change

³ Federal Reserve Major Currency Index, 1973=100 - Quarter End

⁴ Millions of Units

⁵ Annual Numbers Represent Averages

Source: U.S. Department of Commerce, U.S. Department of Labor, Federal Reserve Board, IHS Global Insight and Wells Fargo Securities, LLC

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Together we'll go far



U.S. Review

Signs of Expansion Abound

Nearly every major economic indicator released this week pointed to an expanding U.S. economy. The massive 321,000-payroll gain in November was by far the biggest news. Most industries saw employment gains accelerate in the month, most notably in construction, retail trade, financial activities and professional & business services. The household survey did not corroborate the payroll number's good news, with the unemployment rate inching slightly higher on an unrounded basis. This should not cause alarm, however, as the meager 4,000 workers added in November followed a gargantuan 683,000 workers gained in October, putting the three-month average over 300,000. Average hourly earnings jumped 0.4 percent in the month, though are still up just 2.1 percent year over year. In addition, the work week ticked upward. More jobs, higher wages, longer hours and lower gas prices bode well for the U.S. consumer as we move further into the holiday shopping season.

Although lower energy costs help the consumer, they are a clear challenge to the nation's growing oil and gas industry. According to the Beige Book, oil and gas exploration activity in North Dakota declined early in November and capital expenditures from the Dallas district's energy industry are expected to decline next year. However, the overall outlook for the energy industry in the Dallas district remains positive, and officials in North Dakota anticipate two more years of rising oil production there.

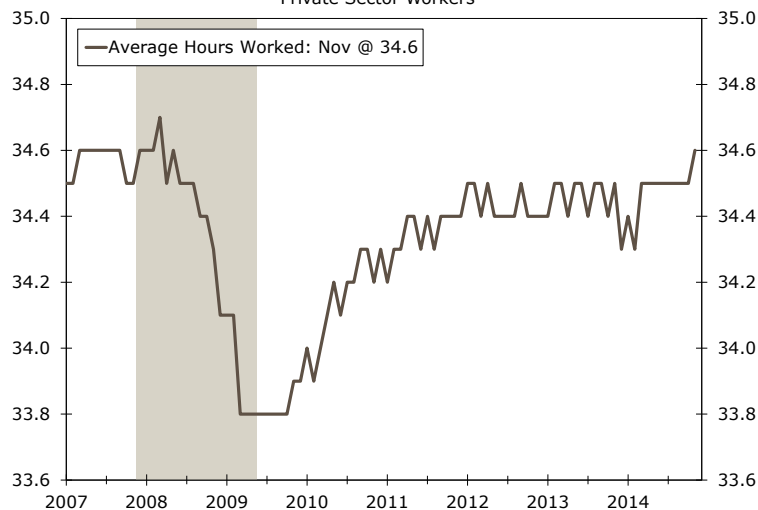
With energy-related industries facing headwinds and poised to decrease their capital expenditures, the rise in new orders out of the ISM manufacturing index came as welcome news. Although the overall index slid slightly to 58.7 in November from 59.0 in the previous month, it still remains firmly in expansion territory. Outside of the energy industry, most businesses benefit from lower oil and gas prices, which may help other manufacturers to pick up some of the slack left by a moderation in oil and gas exploration and production.

The benefit of the drop in oil and other commodity prices has already come through to manufacturers, with the prices paid component of the ISM falling below the critical 50 threshold to 44.5 in November. Price pressures do not appear to have filtered through to other industries just yet, as the prices paid component of the ISM non-manufacturing index actually increased. Weaker price pressures coming down the pipeline give the Fed some breathing room on the timing of a rates liftoff.

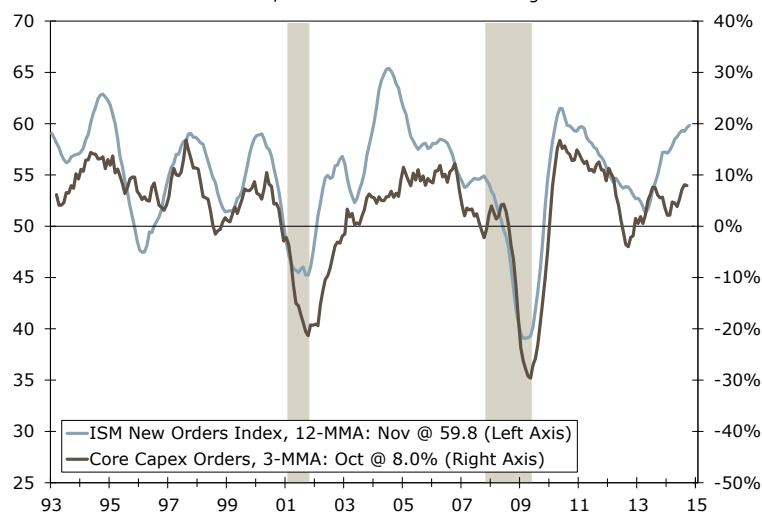
The other major headwind of late comes from the rest of the world as global growth is moderating. Again, the U.S. economy has so far proven to be resilient, with the new export orders component of both the ISM manufacturing and non-manufacturing indices rising in November. In addition, the U.S. trade deficit narrowed slightly in October, though this comes after a sizable widening in September. As we have indicated in other reports, the overall effect of slower global growth should be relatively subdued, as the U.S. economy's exposure to the rest of the world is rather small.

Average Weekly Hours

Private Sector Workers

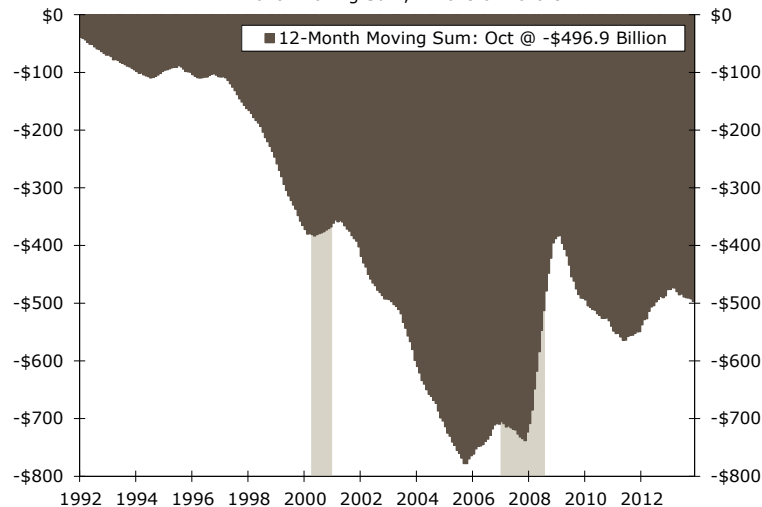


ISM New Orders & Nondef. Cap. Gds. Orders Ex. Aircraft Index, Year-over-Year Percent Change



U.S. Trade Deficit

12-Month Moving Sum, Billions of Dollars



Source: U.S. Department of Labor, U.S. Department of Commerce, ISM and Wells Fargo Securities, LLC

Job Openings • Tuesday

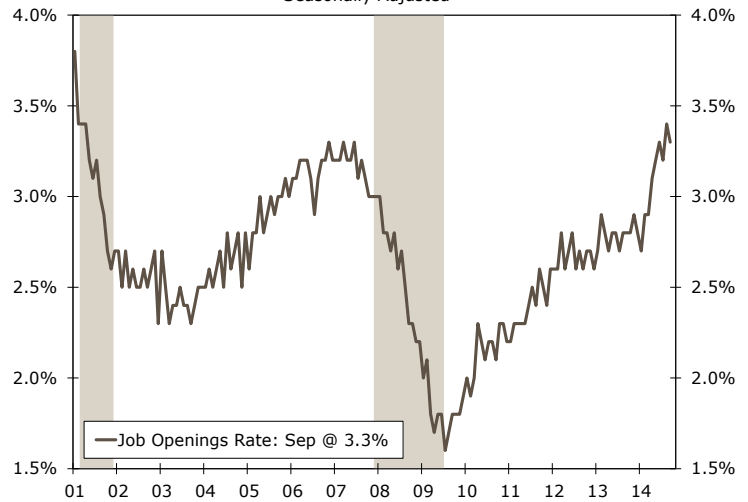
In another sign of improvement in the labor market, turnover in the jobs market is picking up. The gross number of new hires rose to the highest level in nearly six years in September, while the hiring rate—the number of new hires as a share of employment—rose to match the post-recession high reached in July. Separations are rising, but for good reasons as more workers are quitting their jobs. The growing number of quits shows workers are feeling more confident about retiring or changing jobs, which should help with wage growth; workers voluntarily leaving their job often receive higher compensation if moving directly into new employment.

Hiring looks set to strengthen further in the coming months. Although pulling back slightly in September, job openings have risen 20 percent over the past year. Openings likely stayed near recent levels as surveys suggest hiring plans remained relatively strong in recent months.

Previous: 4.74 Million

Consensus: 4.79 Million

Job Openings Rate
Seasonally Adjusted



Retail Sales • Thursday

After falling in September, retail sales rebounded 0.3 percent in October. We expect gains to have continued in November with sales increasing 0.3 percent over the month. Headline sales should be boosted by a nice pickup in autos after unit sales rose to a 17.1 million annualized rate from 16.4 million in October. Another drop in gas prices, however, would push spending at gasoline stations lower and weigh on the headline.

The November retail sales report will be the first real tell of how the holiday shopping season is shaping up. Reports of Black Friday sales were generally disappointing, but in the past have had little correspondence with actual sales figures. We look for “core” retail sales, which exclude autos, gasoline and building materials, to have risen 0.1 percent in November.

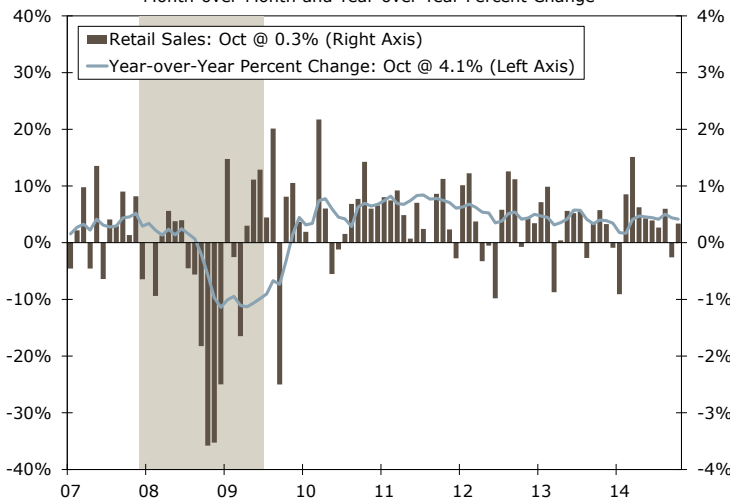
Previous: 0.3%

Wells Fargo: 0.3%

Consensus: 0.4% (Month-over-Month)

U.S. Retail Sales

Month-over-Month and Year-over-Year Percent Change



Producer Price Index • Friday

Discussions of inflation have turned to disinflation in recent months as falling commodity prices have weighed on price growth. The Producer Price Index for final demand unexpectedly rose in October, but the increase was largely attributable to a rise in margins for wholesalers and retailers—a quirk of the new PPI design. Excluding trade services, prices fell 0.2 percent. We expect another drop in oil prices and less favorable margins to lead to a 0.1 percent decline in the PPI for November.

We will also get a look at import prices. Import prices have fallen for four consecutive months following lower prices for fuel products and a stronger dollar. We look for import prices to have fallen an additional 1.8 percent in November and to continue to weigh on domestic inflation.

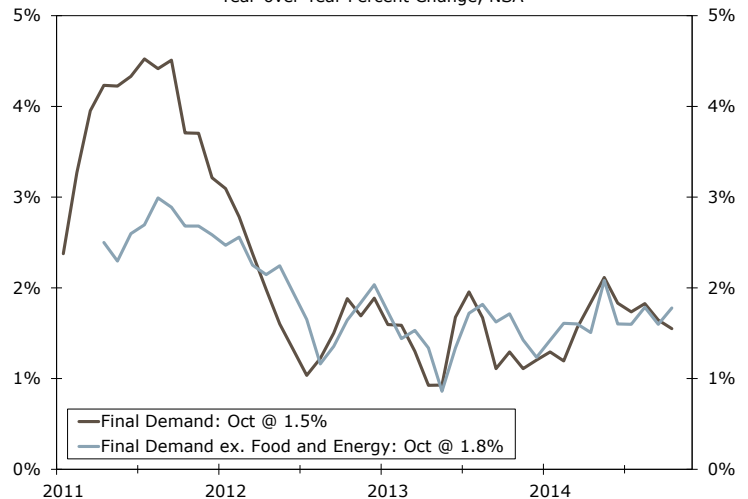
Previous: 0.2%

Wells Fargo: -0.1%

Consensus: -0.1% (Month-over-Month)

PPI and Core PPI Final Demand

Year-over-Year Percent Change, NSA



Source: U.S. Department of Labor, U.S. Department of Commerce and Wells Fargo Securities, LLC

Global Review

Brazilian Central Bank Pushes Forward

The Brazilian central bank surprised markets in late October, just days after the second round of presidential elections, when it raised the Selic benchmark interest rate by 25 bps. The central bank sent an even stronger signal to markets on Dec 3, pushing the Selic rate 50 bps higher to take it to 11.75 percent, in an attempt to keep a lid on the Brazilian currency and inflation expectations.

What is even more telling is that the latest measures come at a time when the Brazilian economy is not growing at all, which means that this further increase in the interest rate is going to put more downward pressure on domestic consumption, making the prospects for a recovery in 2015 highly unlikely. This increase in interest rates also comes days after President Rousseff picked Joaquim Levy, a fiscally conservative economist that served under ex-President Da Silva, as the finance minister to replace Guido Mantega.

The current shift in policy direction from what President Rousseff followed during her first term in office could be signaling a larger influence by ex-President Da Silva on the Rousseff administration. If this is the case, President Rousseff would be relying less on Worker Party's ideologues and more on Lula da Silva's more centrist approach to conducting policy. The biggest problem they will face compared to Lula's eight years in office is the completely different global commodity and growth environment, which will reduce the degrees of freedom from the administration and could limit the ability for tighter fiscal and monetary policy to do the trick.

U.K. PMIs, Economy Remain Strong

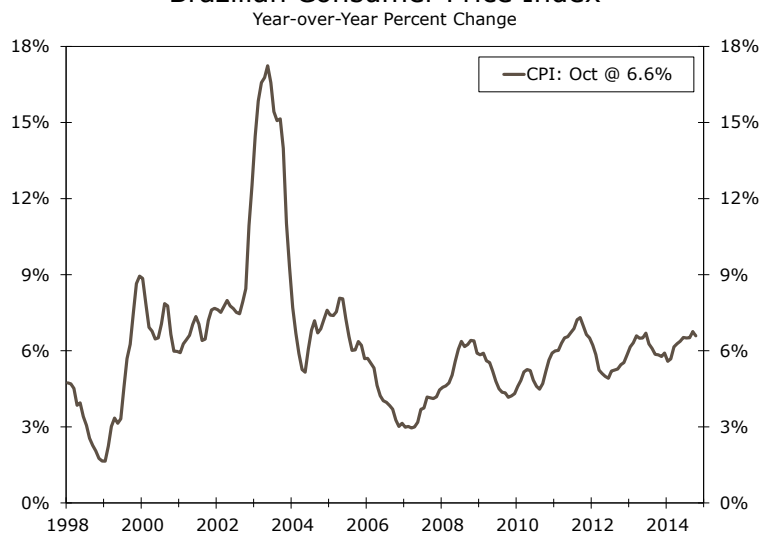
The U.K. economy showed, once again, that it is possible to grow at a relatively strong rate even in the face of a very weak global economic environment, very similarly to what is occurring in the U.S. economy. This was very clear with the release of the PMIs for the month of November, which came in stronger than the previous month as well as stronger than market expectations. The manufacturing index was up to 53.5 compared to expectations of 53.0, while the services index surged to 58.6 from a previous reading of 56.2, above market expectations of 56.5.

Meanwhile, the Bank of England did as expected, staying the course and keeping the degree of monetary expansion unchanged during its December monetary policy meeting.

Mexican PMIs Mixed in November

In Mexico, official PMI readings disappointed in November, with both the manufacturing index and the services index coming in lower than market expectations as well as lower than the October readings. The IMEF manufacturing index weakened to 53.0 from a revised 54.6 reading in October, while the services IMEF went down to 51.2 from a revised reading of 52.1. However, the HSBC manufacturing index went in the other direction by posting a reading of 54.3 compared to a 53.3 reading for October. We believe that the Mexican economy is not as strong as some think it is, and this is being reflected on the Mexican peso, which has taken a beating during the past several weeks.

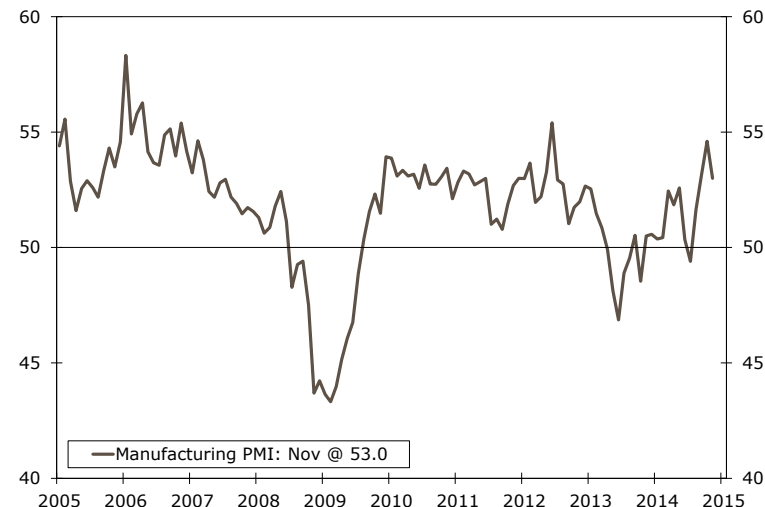
Brazilian Consumer Price Index



U.K. Purchasing Managers' Indices



Mexico IMEF Manufacturing Index



Source: IHS Global Insight, Bloomberg LP and Wells Fargo Securities, LLC

German Industrial Production • Monday

Germany is the largest economy in the Eurozone, so analysts often look at the country as a bellwether for the rest of the euro area. And the slowdown in the German economy over the past two quarters has gone hand-in-hand with deceleration in economic activity in the Eurozone. There are some indications that perhaps growth is picking up a bit. German industrial production (IP) rose 1.4 percent in September, giving it some much-needed upward momentum coming into Q4. Although the consensus forecast anticipates that IP was flat in October, strong increases in factory orders in September (1.1 percent) and October (2.5 percent) suggest that German IP may soon turn up on a sustained basis. Data on exports in October will provide more insights into the present state of the German economy. IP data for the overall euro area are slated for release on Friday.

Previous: 1.4% (Month-over-Month)

Consensus: 0.4%

Chinese Industrial Production Index
Year-over-Year Percent Change of 3-Month Moving Average



Mexican Industrial Production • Friday

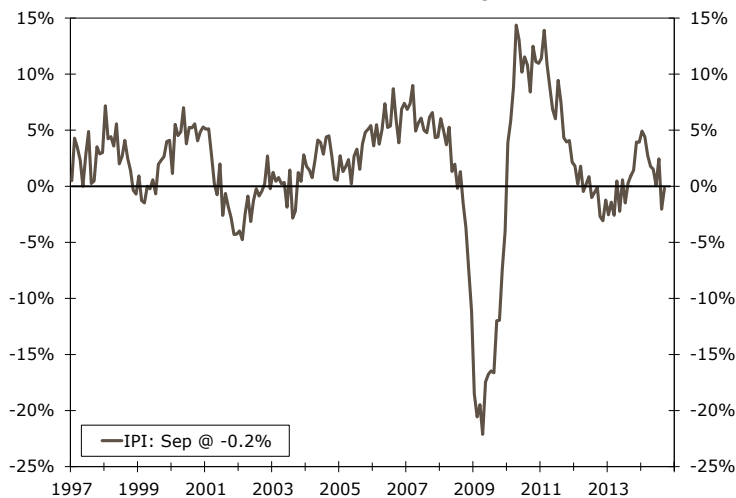
Data on Mexican IP can be choppy, even on a year-over-year basis, but the trend in IP growth in Mexico this year has been positive. With three-quarters of its exports destined for the United States, economic momentum in America obviously is important in determining the rate of IP growth south of the border. With U.S. growth remaining solid, IP growth in Mexico should continue to trend higher in coming months, even if the consensus forecast looks for some slowing in October relative to the previous month.

Data on CPI inflation in October will print on Friday. The overall rate of CPI inflation in Mexico has risen somewhat over the past few months, but analysts look for the year-over-year rate to edge down to 4.2 percent in October from 4.3 percent in September. However, the 10 percent depreciation of the peso against the U.S. dollar since late July makes significant disinflation in Mexico unlikely in coming months.

Previous: 3.0% (Year-over-Year)

Consensus: 2.6%

German Industrial Production Index
Year-over-Year Percent Change



Chinese Industrial Production • Friday

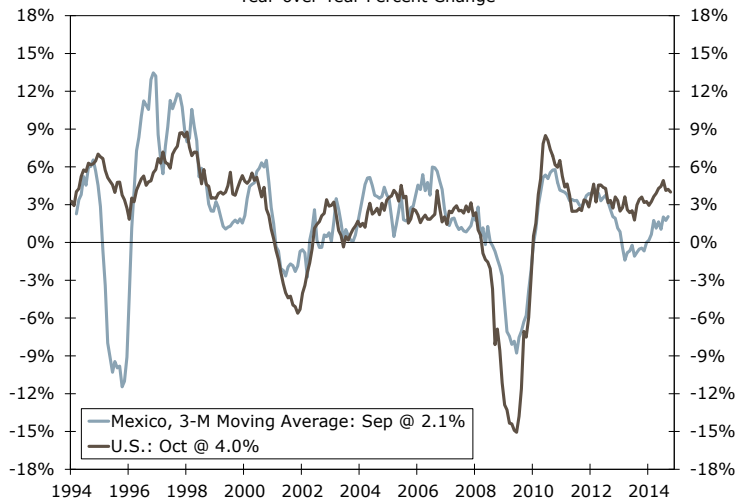
Due to the importance of manufacturing in China—the manufacturing sector accounts for about 40 percent of value-added in the Chinese economy—data on industrial output are important when trying to divine the direction of the Chinese economy. In that regard, the slowdown in IP growth recently suggests that overall economic activity in the world's second-largest economy continues to decelerate. November data on Chinese IP are slated for release on Friday, and the consensus forecast anticipates that the year-over-year rate of IP growth slowed further in November relative to the previous month.

Other data releases on the docket next week, including trade data (Monday) and retail sales (Friday), will impart more information about the state of the Chinese economy in November. In addition, data on bank lending and aggregate financing will help analysts determine near-term growth prospects in China.

Previous: 7.7% (Year-over-Year)

Consensus: 7.5%

Industrial Production Indices
Year-over-Year Percent Change



Source: IHS Global Insight, Federal Reserve Board and Wells Fargo Securities, LLC

Interest Rate Watch

Staying with the Fundamentals

Fundamentals continue to dictate that benchmark U.S. Treasury rates will remain modest despite the advanced age of the economic expansion. Time does not dictate the path of interest rates.

For the year ahead, our real GDP growth expectations revolve around trend growth of 2.75 percent with gains in consumer spending, business investment and government spending. We expect inflation, measured by the PCE deflator, to average just 1.6 percent. This pace of inflation is considerably below what one would see by examining earlier economic expansions.

A Different Policy Reaction Function

In recent weeks, there have been a few commentaries that plot the path of interest rates over recent economic cycles. Given that current rates are far below the average of prior cycles, there is the implication that the aggregate increase in the fed funds target rate will be greater this time around to reassume levels consistent with prior cycles. We disagree.

A significant difference in this cycle is that the Federal Open Market Committee (FOMC) is reacting very cautiously to the gap between actual and targeted inflation and the improvement in the labor market. For example, the rapid drop in the unemployment rate to what is perceived by some to be near full-employment has not led to any move by the FOMC to raise the funds rate. Meanwhile, inflation remains low relative to past economic expansions. Moreover, the bias on policy appears to be more focused on getting inflation up, while allowing the unemployment rate to continue to decline. Therefore, we expect FOMC members to reduce their projected fed funds rate targets for the end of 2015 and 2016 in the months ahead.

Complication of an Exit from ZIRP

In prior notes, we have argued that the technical difficulties and market liquidity issues associated with the FOMC exit from the zero interest rate policy (ZIRP) would further limit Fed actions. Therefore, we suspect the historical degree of interest rate increases in prior cycles will not be repeated.

Credit Market Insights

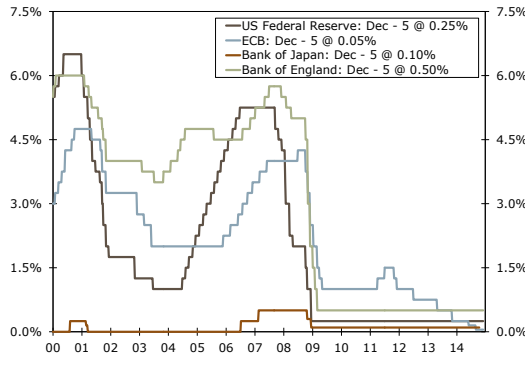
FDIC Quarterly Banking Profile

The FDIC Quarterly Banking Profile (QBP) gives us a snapshot of the aggregate financial position of insured institutions. We have seen broad improvements since the financial crisis, and this trend continued in the third quarter.

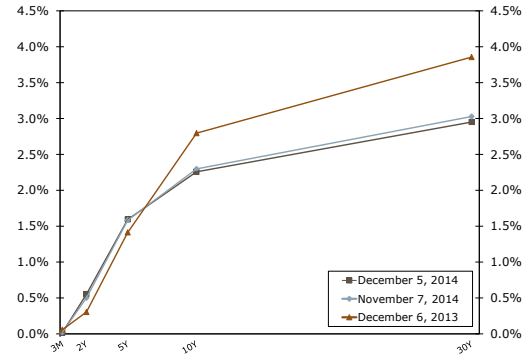
The third quarter saw a continued decline in noncurrent loan and lease balances, which fell almost \$10 billion, or 5.3 percent. The number of loans and leases 30 to 89 days past due is approaching prerecession “normal” levels, but the number of loans 90 or more days past due remain quite elevated. All major components fell over the quarter except for loans to individuals. This increase was driven by increases in noncurrent balances on credit cards (up \$275 million) and auto loans (up \$99 million). Noncurrent mortgages declined the most over the month. We view the continued decline in noncurrent loan balances as an indication that the balance sheets of households and firms continue to improve.

The QBP also indicated that banks’ holdings of Treasury securities continued to increase in the third quarter. In our view, the demand for Treasuries by banks has, at least partially, resulted from increased regulation and capital requirements. We feel this has been a major reason for the continued low yields on these instruments.

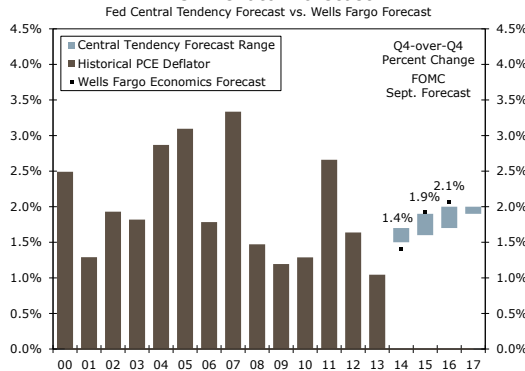
Central Bank Policy Rates



Yield Curve U.S. Treasuries, Active Issues



PCE Deflator Forecast



Source: IHS Global Insight, Bloomberg LP and Wells Fargo Securities, LLC

Credit Market Data

Mortgage Rates	Current	Week	4 Weeks	Year
		Ago	Ago	Ago
30-Yr Fixed	3.89%	3.97%	4.01%	4.46%
15-Yr Fixed	3.10%	3.17%	3.20%	3.47%
5/1 ARM	2.94%	3.01%	3.02%	2.99%
1-Yr ARM	2.41%	2.44%	2.43%	2.59%

Bank Lending	Current Assets (Billions)	1-Week	4-Week	Year-Ago
		Change (SAAR)	Change (SAAR)	Change
Commercial & Industrial	\$1,759.4	24.75%	11.37%	12.99%
Revolving Home Equity	\$459.6	-1.59%	-0.95%	-3.45%
Residential Mortgages	\$1,575.1	11.79%	-10.07%	0.49%
Commercial Real Estate	\$1,582.6	0.60%	1.16%	6.37%
Consumer	\$1,198.2	0.93%	6.02%	5.44%

Source: Freddie Mac, Federal Reserve Board and Wells Fargo Securities, LLC

Topic of the Week

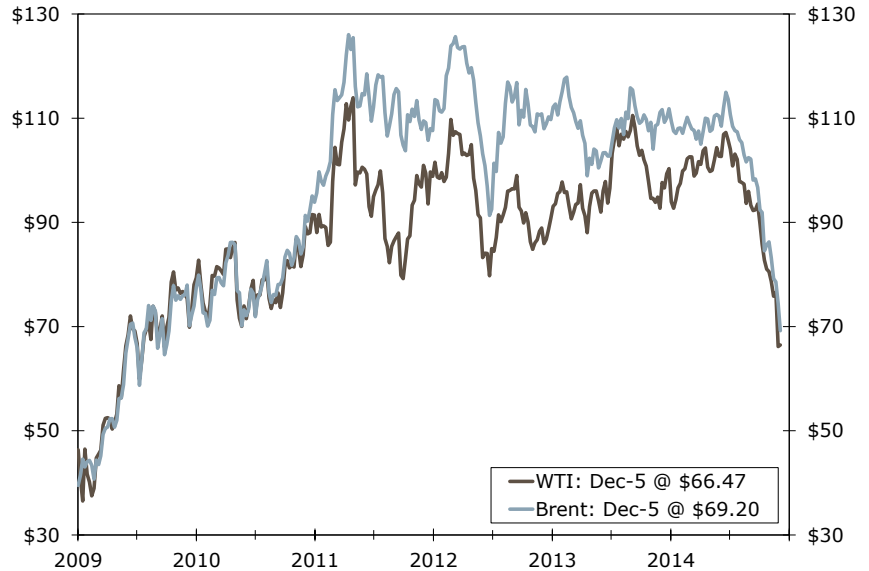
Crude Economics

As of this morning, the prices of WTI and Brent were at \$66.47 and \$69.20 per barrel, respectively, both more than 30 percent off June levels (top chart). Neither Brent nor WTI has been priced this low since early 2010. Given the surge in output in the past few years by domestic shale producers, a great deal of attention has been paid to breakeven oil prices for individual shale plays. Some analysts suggest that oil prices are approaching or have already fallen below breakeven levels for some shale plays, and that supply may tighten as some of these producers are cut out of the market. Although many energy analysts have published estimates of breakeven prices for individual basins, our in-house analysts at Wells Fargo acknowledge that calculating these prices is more art than science. A plethora of constantly-changing variables, including hedging, leverage and input costs, make nailing down a hard number nearly impossible. For our purposes, we focus on the effects of cheap oil on the broader economy.

As we take stock of the winners and losers from lower oil prices, the clearest winner is the consumer. Lower gas prices free up real disposable income, which is a potential lift for both holiday sales and the broader real PCE outlook. However, for players in the North American shale boom, the situation is not as bright. While shale companies are less likely to cut production in the near term as they attempt to recoup their fixed costs, they may first look to trim their capex as a means of improving cash flow. Oil and gas capex has recently been a key driver of growth in equipment spending, the category that has provided the most outsized contribution to growth in business fixed investment (BFI) in the past few years (bottom chart). On that basis, we have pared back our outlook for BFI for the current quarter and the first quarter of next year.

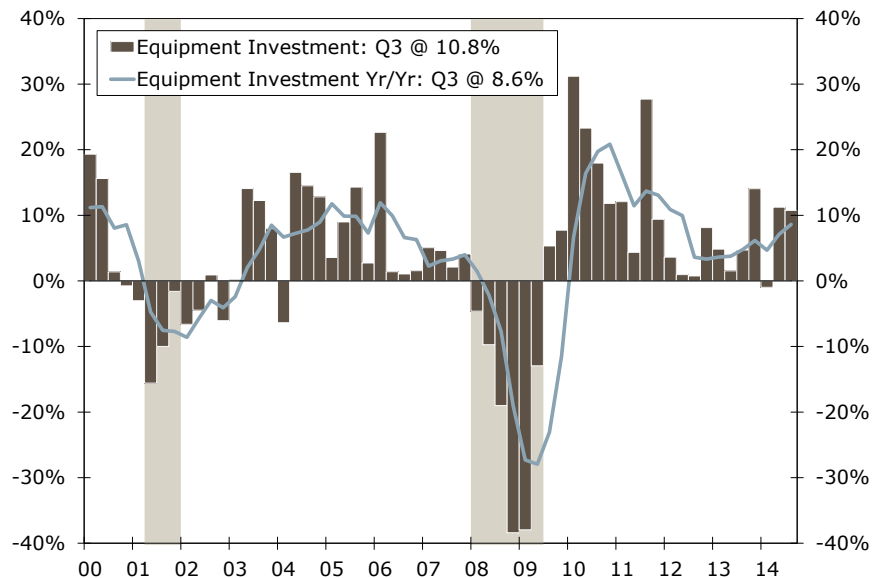
For further discussion, see our report *"Equipment Spending Prospects Fall With Oil Prices,"* available on our website.

World Oil Prices
Cash Spot Prices, Dollars per Barrel



Real Business Fixed Investment, Equipment

Bars = Compound Annual Rate Line = Yr/Yr % Change



Source: U.S. Department of Commerce, IHS Global Insight and Wells Fargo Securities, LLC

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Market Data ♦ Mid-Day Friday

U.S. Interest Rates

	Friday 12/5/2014	1 Week Ago	1 Year Ago
3-Month T-Bill	0.02	0.01	0.06
3-Month LIBOR	0.24	0.23	0.24
1-Year Treasury	0.18	0.15	0.14
2-Year Treasury	0.64	0.47	0.30
5-Year Treasury	1.69	1.48	1.49
10-Year Treasury	2.32	2.16	2.87
30-Year Treasury	2.98	2.89	3.91
Bond Buyer Index	3.83	3.94	4.70

Foreign Exchange Rates

	Friday 12/5/2014	1 Week Ago	1 Year Ago
Euro (\$/€)	1.230	1.245	1.367
British Pound (\$/£)	1.559	1.565	1.633
British Pound (£/€)	0.789	0.796	0.837
Japanese Yen (¥/\$)	121.500	118.630	101.790
Canadian Dollar (C\$/\\$)	1.143	1.142	1.065
Swiss Franc (CHF/\$)	0.978	0.965	0.897
Australian Dollar (US\$/A\$)	0.833	0.851	0.906
Mexican Peso (MXN/\$)	14.299	13.929	13.090
Chinese Yuan (CNY/\$)	6.152	6.145	6.092
Indian Rupee (INR/\$)	61.785	62.033	61.765
Brazilian Real (BRL/\$)	2.604	2.565	2.357
U.S. Dollar Index	89.272	88.356	80.235

Source: Bloomberg LP and Wells Fargo Securities, LLC

Foreign Interest Rates

	Friday 12/5/2014	1 Week Ago	1 Year Ago
3-Month Euro LIBOR	0.06	0.06	0.20
3-Month Sterling LIBOR	0.56	0.55	0.52
3-Month Canada Banker's Acceptance	1.28	1.28	1.28
3-Month Yen LIBOR	0.11	0.11	0.15
2-Year German	-0.02	-0.03	0.21
2-Year U.K.	0.57	0.51	0.50
2-Year Canadian	1.05	0.99	1.09
2-Year Japanese	0.00	0.01	0.09
10-Year German	0.78	0.70	1.86
10-Year U.K.	2.02	1.93	2.92
10-Year Canadian	1.96	1.86	2.68
10-Year Japanese	0.42	0.42	0.63

Commodity Prices

	Friday 12/5/2014	1 Week Ago	1 Year Ago
WTI Crude (\$/Barrel)	65.47	66.15	97.38
Gold (\$/Ounce)	1193.71	1167.41	1225.17
Hot-Rolled Steel (\$/S.Ton)	620.00	629.00	676.00
Copper (¢/Pound)	292.80	286.00	326.15
Soybeans (\$/Bushel)	10.08	10.42	13.32
Natural Gas (\$/MMBTU)	3.75	4.09	4.13
Nickel (\$/Metric Ton)	17,055	16,302	13,592
CRB Spot Inds.	503.87	506.06	524.02

Next Week's Economic Calendar

	Monday 8	Tuesday 9	Wednesday 10	Thursday 11	Friday 12
U.S. Data		Wholesale Inventories (MoM) September 0.3% October 0.1% (C)		Retail Sales (MoM) October 0.3% November 0.3% (W)	PPI Final Demand (MoM) October 0.2% November -0.1% (W)
				Import Price Index (MoM) October -1.3% November -2.8% (W)	
	Germany Industrial Production (MoM) Previous (September) 1.4%	Japan PPI (YoY) Previous (October) 2.9%	Australia Unemployment Rate Previous (October) 6.2%		China Industrial Production (YoY) Previous (October) 7.7%
		United Kingdom Industrial Production (MoM) Previous (September) 0.6%			Mexico Industrial Production (YoY) Previous (September) 2.6%

Note: (W) = Wells Fargo Estimate (C) = Consensus Estimate

Source: Bloomberg LP and Wells Fargo Securities, LLC

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