

# U.S. Outlook

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Date	Indicator	For	Estimate	Consensus*	Previous Period
27-January -2015	Durable Goods Orders	DEC	0.5%	0.5%	-0.9%
27-January -2015	Durables Ex Transportation	DEC	0.6%	0.6%	-0.7%
27-January -2015	S&P Case-Shiller 20-City Index MoM	NOV	0.8%	0.67%	0.76%
27-January -2015	New Home Sales	DEC	445K	450K	438K
27-January -2015	Consumer Confidence Index	JAN	94.2	95.0	92.6
28-January -2015	FOMC Rate Decision – Upper Bound	JAN	0.25	0.25	0.25
28-January -2015	FOMC Rate Decision – Lower Bound	JAN	0.00	0.00	0.00
29-January -2015	Initial Jobless Claims	01/24	310K	300K	307K
29-January -2015	Pending Home Sales MoM	DEC	0.4%	0.5%	0.8%
30-January -2015	Employment Cost Index	Q4	0.6%	0.6%	0.7%
30-January -2015	GDP Annualized QoQ - Advance	Q4	3.2%	3.3%	5.0%
30-January -2015	Personal Consumption	Q4	3.8%	4.2%	3.2%
30-January -2015	GDP Price Index	Q4	1.0%	1.0%	1.4%
30-January -2015	Chicago Purchasing Manager Index	JAN	58.2	58.0	58.8
30-January -2015	Univ. of Michigan Sentiment - Final	JAN	98.0	98.2	98.2

\*Consensus from Bloomberg

## Deflation Fight Moves Overseas

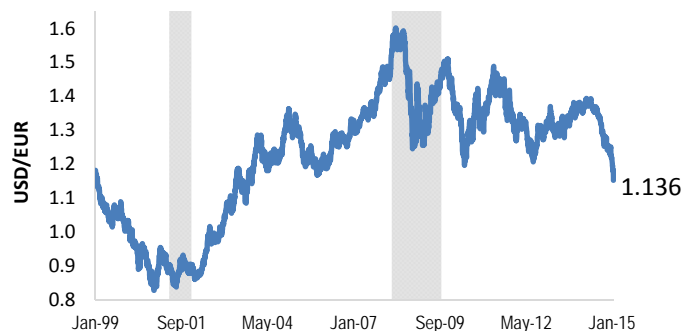
After three rounds of quantitative easing, the Fed is remaining on the sidelines as global central banks from the ECB, Canada, Peru, Switzerland, Denmark and India all made moves this month to loosen monetary policy and head off economic and deflation risks.

The ECB's launch of its own QE asset purchase program stole the headlines and will have the farthest reaching implications for the global economy, markets, and the United States.

My first observation of the ECB's dramatic move is that the asset purchases of 60 billion euros per month starting in March, 1.1 trillion euros in total through September of 2016, are in the right ballpark to improve Europe's economic and inflation outlook. Initial market reactions from stocks, bonds, and the euro have been encouraging and will be a net positive for European growth prospects. But one of the most attractive features of asset purchase program is that it is open-ended should additional asset purchases be needed.

## Euro Declines Will Bolster Europe's Exports & Prices

### U.S. / Euro Foreign Exchange Rate



Source: Federal Reserve System

The drop in the euro is the most helpful outcome of this week's market action. The euro dropped more than 2.0 percent on Thursday and has fallen 9.2 percent against the U.S. dollar since December 16, and 19 percent against the U.S. dollar since last March. A weaker euro will bolster Europe's exports, tourism, and transportation industries, while helping to stabilize Eurozone prices. It's like a 20-percent-off coupon for foreign buyers of the Eurozone's goods and services. At the same time, a weaker euro blunts oil price declines in euros and will

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raise import prices on a whole range of other imported goods, getting the ECB closer to its goals on the economy and inflation. While not a complete panacea for what ails the Eurozone, the ECB's QE is a significant step in the right direction.

From a U.S. perspective, the ECB's actions take away the worst case economic and deflation scenario for the Eurozone. By doing so, it reduces the risk of financial contagion from the Eurozone to the U.S., which solidifies our outlook for a relatively robust U.S. economy this year.

While all eyes have been focused on Europe, the U.S. 10-Year Treasury yield has risen about 15 basis points over the last two weeks with spreads against German Bunds widening to 142 basis points from 124 basis points in mid-January, which I take as a sign that the global flight to safety trade is unwinding, and global deflation risks have diminished a bit with these actions.

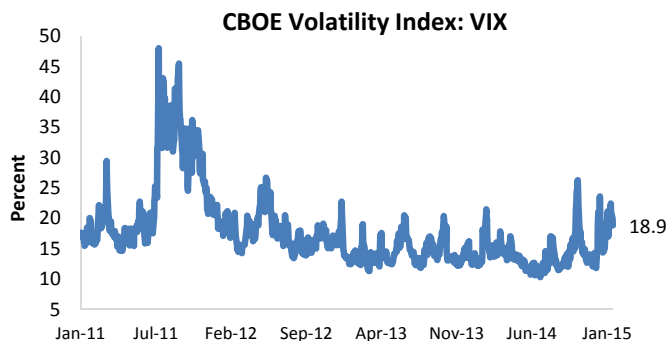
#### Long-term Treasury Yields Bounce Higher On The News



Source: Federal Reserve System

As if on cue, the VIX index a market measure of future stock market price volatility slipped to 16.4, not far from its six month average and down from a January peak of 22.4 – another sign financial crisis fears have subsided.

#### The VIX Settles Back Down

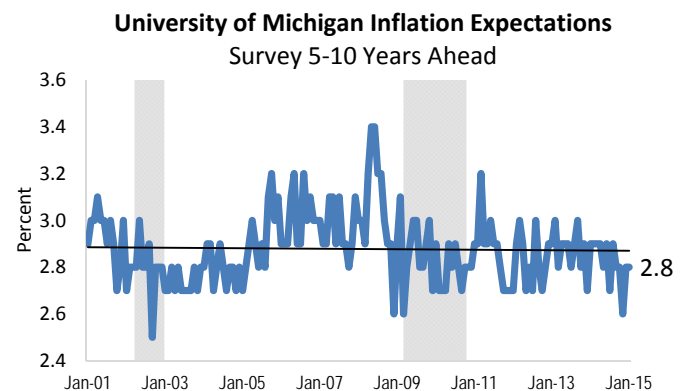


Source: Chicago Board Options Exchange

Finally, the ECB decision yesterday makes a Fed mid-2015 liftoff date for the Fed funds target rate more likely. With the ECB now more forcefully addressing deflation risks there, the Fed will feel less pressure to delay rate hikes in the United States. This makes the Fed's current short-term interest rate normalization plans more likely to be executed on time this year. We still see the June FOMC meeting as the most likely date for Fed Funds target rate liftoff.

So with global central banks reapplying the monetary policy accelerator, why is the Fed likely to sit this one out? In short, the Fed monetary policy goals are still squarely in sight. Even if oil prices lead to a temporary bout of deflation here in the United States, it won't last and is not likely to lead to adverse outcomes for domestic demand unless future inflation expectations and wages follow oil prices lower. As the FOMC has often noted in their statements, longer-term inflation expectations remain stable.

#### Inflation Expectations 5-10 Years Out Remain Stable



Source: Thomson Reuters/Univ. Of Michigan

What could get the FOMC to hold its fire and delay liftoff this year? Barring widespread financial crisis or a pull-back in wage growth, I have trouble seeing any. Of particular interest this coming week will be the Employment Cost Index for the fourth quarter released next Friday. This measure of labor market compensation has been trending higher over the past two quarters at its fastest clip since the first half of 2008. Any significant reversal in that positive trend, especially in light of the weaker-than-expected average hourly earnings growth in December's payroll report, could give the members of the FOMC some more reasons to wait a while longer. But, even that scenario seems unlikely in my view.

## Major Economic Indicators

Economic Data	History				Forecast								Yr/Yr % chg or Annual Avg.			
	2014.1	2014.2	2014.3	2014.4	2015.1	2015.2	2015.3	2015.4	2016.1	2016.2	2016.3	2016.4	2013	2014	2015	2016
Real GDP*	-2.1	4.6	5.0	3.2	2.5	2.7	3.1	3.1	2.6	2.9	2.5	2.6	2.2	2.5	3.2	2.8
Personal Consumption Expenditures*	1.2	2.5	3.2	3.8	3.2	3.3	3.5	3.4	2.9	2.9	2.5	2.4	2.4	2.5	3.4	3.0
Non-residential Fixed Investment*	1.6	9.7	8.9	2.5	5.0	5.0	5.0	5.0	4.7	4.6	4.6	4.2	3.0	6.2	5.3	4.8
Private Housing Starts (000s units)	925	985	1,033	1,039	1,070	1,100	1,121	1,143	1,165	1,180	1,240	1,260	930	996	1,109	1,211
Vehicle Sales (mill. Units, annualized)	15.6	16.5	16.7	16.8	17.0	17.1	17.2	17.2	17.2	17.2	17.3	17.3	15.5	16.4	17.2	17.2
Industrial Production*	3.9	5.7	4.0	5.0	3.5	3.3	3.3	3.2	3.4	3.4	3.4	3.4	2.9	4.2	3.9	3.4
Nonfarm Payroll Employment (mil.)	137.8	138.5	139.2	140.1	140.8	141.5	142.1	142.8	143.5	144.1	144.8	145.4	136.4	138.9	141.8	144.4
Unemployment rate	6.7	6.2	6.1	5.7	5.5	5.4	5.3	5.2	5.2	5.1	5.0	5.0	7.4	6.2	5.4	5.1
Consumer Price Index* (percent)	1.9	3.0	1.1	-1.2	-3.5	1.7	1.9	1.9	1.9	1.9	2.0	2.1	1.5	1.6	-0.1	1.9
"Core" CPI* (percent)	1.6	2.5	1.3	1.4	1.2	1.5	1.5	1.6	1.7	1.7	1.8	1.8	1.8	1.7	1.5	1.7
PPI (finished goods)* (percent)	3.9	3.9	0.8	-5.6	-4.7	0.3	1.0	1.1	1.3	1.3	1.4	1.4	1.2	1.9	-1.7	1.2
Trade Weighted Dollar (Fed BOG, major)	76.9	76.4	77.5	82.2	87.0	87.5	88.4	88.7	89.0	89.8	90.5	90.4	76.1	78.3	87.9	89.9
Crude Oil Prices -WTI (\$ per barrel)	99	103	98	76	50	53	58	60	68	69	70	71	98	94	55	70

\*Quarterly Data Percent Change At Annual Rate; Annual Data Year-on-Year % Chg, or Annual Average.

Financial Data	History				Forecast								Annual Average			
	2014.1	2014.2	2014.3	2014.4	2015.1	2015.2	2015.3	2015.4	2016.1	2016.2	2016.3	2016.4	2013	2014	2015	2016
S & P 500	1,835	1,900	1,976										1,644			
Dow Jones Industrial Average	16,177	16,604	16,954										15,010			
Federal Funds Rate (effective)	0.07	0.09	0.09	0.08	0.10	0.18	0.43	0.70	1.12	1.37	1.62	1.95	0.11	0.08	0.35	1.52
Treasury-3 Month Bills (yield)	0.05	0.03	0.03	0.02	0.03	0.16	0.43	0.76	1.17	1.42	1.67	2.00	0.06	0.03	0.35	1.57
Treasury-2 Year Notes (yield)	0.37	0.42	0.52	0.52	0.52	0.65	0.93	1.13	1.60	1.90	2.15	2.48	0.31	0.45	0.81	2.03
Treasury-5 Year Notes (yield)	1.60	1.66	1.70	1.57	1.40	1.61	1.82	2.10	2.57	2.77	3.02	3.15	1.17	1.63	1.73	2.88
Treasury-10 Year Notes (yield)	2.77	2.62	2.50	2.27	2.00	2.25	2.46	2.61	2.81	2.94	3.05	3.28	2.35	2.54	2.33	3.02
Treasury-30 Year Notes (yield)	3.68	3.44	3.27	2.97	2.60	2.73	2.90	3.00	3.21	3.32	3.50	3.58	3.44	3.34	2.81	3.40
Prime Rate	3.25	3.25	3.25	3.25	3.25	3.25	3.43	3.70	4.12	4.37	4.62	4.95	3.25	3.25	3.41	4.52
Libor 3-Mo. U.S. Dollar	0.26	0.25	0.24	0.23	0.24	0.27	0.48	0.80	1.21	1.47	1.71	2.05	0.28	0.25	0.45	1.61
Mortgage-30 Year (yield)	4.36	4.23	4.14	4.03	3.81	4.07	4.31	4.45	4.62	4.75	4.86	5.09	3.98	4.19	4.16	4.83
BAA Corporate (yield)	5.12	4.82	4.74	4.74	4.58	4.68	4.86	5.02	5.25	5.40	5.52	5.75	5.10	4.86	4.79	5.48

Source: Bank of the West Economics, Bloomberg, Federal Reserve