

U.S. Outlook

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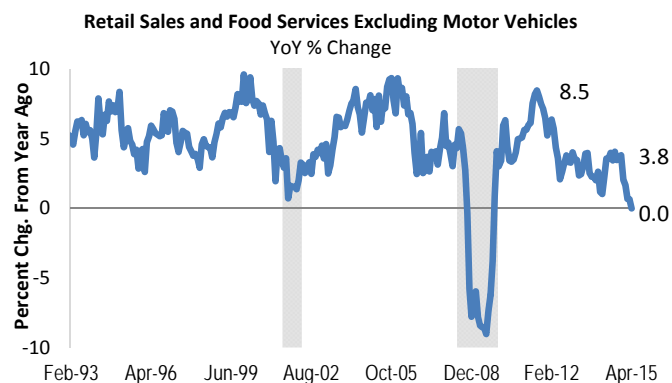
Date	Indicator	For	Estimate	Consensus*	Previous Period
18-MAY-2015	NAHB Housing Market Index	May	55	56	56
19-MAY-2015	Housing Starts	Apr	1025K	1020K	926K
19-MAY-2015	Building Permits	Apr	1066K	1063K	1042K
20-MAY-2015	Fed Minutes from April FOMC Meeting	NA	NA	NA	NA
21-MAY-2015	Chicago Fed Nat Activity Index	Apr	NA	NA	-0.42
21-MAY-2015	Initial Jobless Claims	16-May	NA	NA	NA
21-MAY-2015	Philadelphia Fed Business Outlook	May	8.5	8.0	7.5
21-MAY-2015	Existing Home Sales	Apr	5.24M	5.22M	5.19M
21-MAY-2015	Leading Index	Apr	0.1%	0.2%	0.2%
21-MAY-2015	Markit US Manufacturing PMI	May P	54.7	54.4	54.1
22-MAY-2015	CPI MoM	Apr	0.1%	0.1%	0.2%
22-MAY-2015	CPI Ex Food and Energy MoM	Apr	0.2%	0.2%	0.2%

*Consensus from Bloomberg

Consumers Still Holding Back in April

We can't blame bad weather for another month of disappointing retail sales. The April retail sales numbers continued to disappoint, suggesting weaker real consumer spending growth in Q2 than previously expected. A stronger consumer is needed to offset weak business investment and declining exports. At least through April it appears the rebound from Q1's dismal real GDP growth rate will remain anemic. We currently forecast real GDP growth in the second quarter somewhere around 2.3%. This is bad news since recent data releases imply real GDP for the first quarter will be revised to a negative 0.6%. In fact, the first half real GDP growth rate has been so bad that even if growth rebounds toward 3.0% in the second half of the year, the full-year growth rate will be only 2.2% in 2015, roughly same as the average annual growth rate seen over the last five years, and lower than last year's 2.4% performance.

Retail Sales Growth Evaporates Over Last Five Months



Source: U.S. Census Bureau

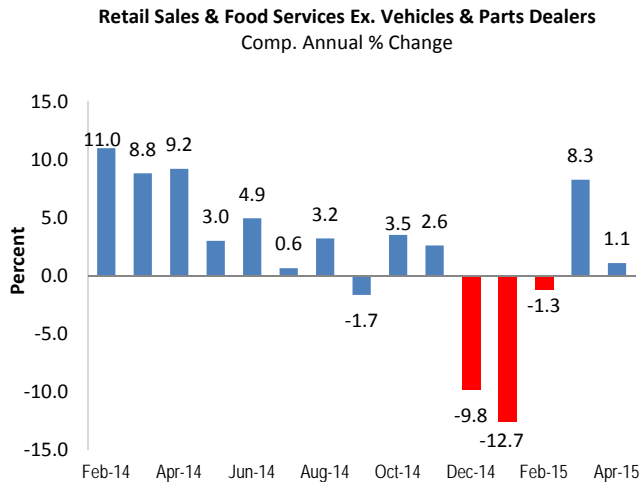
How bad is it? From a year ago retail sales excluding motor vehicles haven't grown at all, something rarely seen in the United States, even during recessions. The last time retail sales growth stumbled this badly was during the "Great Recession". So are we headed for recession? I don't think so. To understand why, let's dive deeper into the retail sales numbers and consider some other economic forces the US economy has working in its favor.

On a monthly basis, retail sales are making a recovery from the winter blues, but it hasn't been strong enough yet

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to make a noticeable dent in the year-on-year growth rate. As you can see in the chart below, over the last two months when winter weather hasn't been a factor, retail sales have trended at an average 4.7% on an annualized basis. A rebound from the first quarter, for sure, but not the monster bounce many economists have been anticipating.

A One Month and Done Retail Sales Rebound?



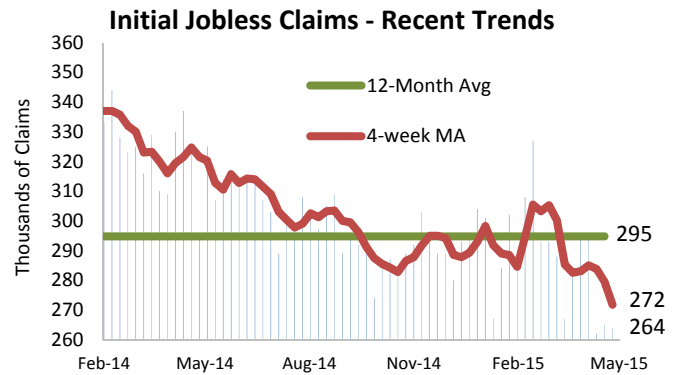
Source: U.S. Census Bureau

In response, we have lowered our forecast for real consumer spending growth in Q2 to 3.2% from 3.8% annualized.

This new-found weakness in retail sales makes the timing of the first U.S. interest rate hike more uncertain. The FOMC, now in data-dependence mode, probably won't chance a rate hike in this anemic economic environment without more concrete signs of acceleration. If the second-half recovery materializes, the FOMC could still move in September, but now there is a rising probability rate hikes could be delayed until the end of the year. Why consumers have stopped spending is the biggest mystery in the U.S. economy today.

It doesn't appear labor market worries are holding back consumers. Initial jobless claims remain extremely low, by historical standards.

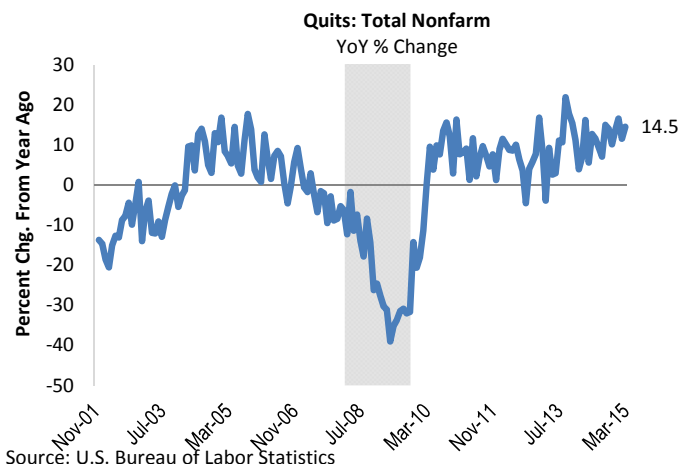
Don't Blame A Weak Labor Market For Consumer Pull-Back



Source: US Employment & Training Administration

Job openings, a leading indicator of job creation, stopped rising last month, but remain 18.6% higher than a year ago. Job quits are also on the rise, up 14.5% from a year ago. This is a sign that workers are becoming more confident in their ability to find better re-employment. It is a vote from workers that the labor market improvement seen over the past year will continue into the future.

Workers Confident Enough to Quit Their Jobs



Source: U.S. Bureau of Labor Statistics

Add in robust stock and home price gains, and lower debt-to-income ratios and it's hard to make a case that consumers will hold back for too much longer.

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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	2.2	-0.6	2.3	3.0	2.9	2.7	2.8	2.7	2.7	2.2	2.4	2.2	2.8
Personal Consumption Expenditures*	1.2	2.5	3.2	4.4	2.0	3.2	3.5	3.4	3.1	3.1	2.9	2.8	2.4	2.5	3.2	3.2
Non-residential Fixed Investment*	1.6	9.7	8.9	4.7	-3.4	-0.2	5.0	5.0	4.7	4.6	4.6	4.2	3.0	6.3	2.9	4.5
Private Housing Starts (000s units)	925	985	1,030	1,063	969	1,040	1,101	1,133	1,145	1,170	1,230	1,250	930	1,001	1,061	1,199
Vehicle Sales (mill. Units, annualized)	15.7	16.5	16.7	16.8	16.6	16.8	17.0	17.1	17.2	17.2	17.3	17.3	15.5	16.4	16.9	17.2
Industrial Production*	3.9	5.7	4.1	4.6	-1.0	2.0	3.3	3.2	3.4	3.4	3.4	3.4	2.9	4.2	2.4	3.3
Nonfarm Payroll Employment (mil.)	137.8	138.6	139.4	140.2	141.0	141.7	142.4	143.1	143.8	144.5	145.2	145.9	136.4	139.0	142.0	144.9
Unemployment rate	6.6	6.2	6.1	5.7	5.6	5.3	5.1	5.0	4.9	4.8	4.8	4.7	7.4	6.2	5.3	4.8
Consumer Price Index* (percent)	2.1	2.4	1.2	-0.9	-3.0	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)	1.8	2.2	1.4	1.5	1.9	1.8	1.8	1.9	1.9	1.9	2.0	2.0	1.8	1.7	1.8	1.9
PPI (finished goods)* (percent)	4.1	3.5	0.4	-5.1	-11.5	0.3	1.0	1.1	1.3	1.3	1.4	1.4	1.2	1.3	0.3	1.8
Trade Weighted Dollar (Fed BOG, major)	76.9	76.4	77.5	82.2	89.3	91.0	91.4	91.7	91.0	91.8	92.5	92.4	76.1	78.3	90.9	91.9
Crude Oil Prices -WTI (\$ per barrel)	99	103	98	73	49	58	60	60	62	63	64	65	98	94	57	64

*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	2,009	2,064								1,644			
Dow Jones Industrial Average	16,177	16,604	16,954	17,345	17,808								15,010			
Federal Funds Rate (effective)	0.07	0.09	0.09	0.10	0.11	0.13	0.21	0.46	0.88	1.13	1.38	1.71	0.11	0.08	0.23	1.27
Treasury-3 Month Bills (yield)	0.05	0.03	0.03	0.02	0.02	0.03	0.11	0.36	0.78	1.03	1.28	1.61	0.06	0.03	0.13	1.18
Treasury-2 Year Notes (yield)	0.37	0.42	0.52	0.54	0.60	0.65	0.88	1.08	1.55	1.85	2.10	2.43	0.31	0.45	0.80	1.98
Treasury-5 Year Notes (yield)	1.60	1.66	1.70	1.60	1.46	1.55	1.72	2.00	2.44	2.64	2.89	3.02	1.17	1.63	1.68	2.75
Treasury-10 Year Notes (yield)	2.77	2.62	2.50	2.28	1.97	2.17	2.35	2.51	2.71	2.84	2.95	3.18	2.35	2.54	2.25	2.92
Treasury-30 Year Notes (yield)	3.68	3.44	3.27	2.97	2.55	2.77	2.95	3.05	3.16	3.27	3.40	3.53	3.44	3.34	2.83	3.34
Prime Rate	3.25	3.25	3.25	3.25	3.25	3.25	3.33	3.58	4.00	4.25	4.50	4.83	3.25	3.25	3.35	4.40
Libor 3-Mo. U.S. Dollar	0.26	0.25	0.24	0.25	0.30	0.30	0.33	0.58	1.00	1.25	1.50	1.83	0.28	0.25	0.38	1.40
Mortgage-30 Year (yield)	4.36	4.23	4.14	3.96	3.72	3.92	4.16	4.30	4.52	4.65	4.76	4.99	3.98	4.19	4.02	4.73
BAA Corporate (yield)	5.12	4.82	4.74	4.73	4.50	4.65	4.78	4.87	5.05	5.20	5.32	5.55	5.10	4.86	4.70	5.28

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