U.S. Outlook

December 4, 2015

SCOTT ANDERSON, Ph.D | Chief Economist | 415.765.8020
www.bankofthewest.com

BANK OF THE WEST | BNP PARIBAS GROUP

Date	Indicator	For	Estimate	Consensus*	Previous Period
7-Dec-2015	Labor Market Conditions Index Change	Nov	NA	NA	1.6
7-Dec-2015	Consumer Credit	Oct	$18.9b	$17.5b	$28.9b
8-Dec-2015	NFIB Small Business Optimism	Nov	NA	NA	96.1
8-Dec-2015	JOLTS Job Openings	Oct	NA	NA	5,526
9-Dec-2015	Wholesale Inventories MoM	Oct	-0.2%	0.0%	0.5%
10-Dec-2015	Import Price Index MoM	Nov	-0.9%	-0.8%	-0.5%
10-Dec-2015	Initial Jobless Claims	05-Dec	266K	NA	269K
10-Dec-2015	Household Change in Net Worth	3Q	NA	NA	$695b
11-Dec-2015	Retail Sales Advance MoM	Nov	0.4%	0.3%	0.1%
11-Dec-2015	Retail Sales Ex Auto MoM	Nov	0.3%	0.3%	0.2%
11-Dec-2015	PPI Final Demand MoM	Nov	-0.2%	0.0%	-0.4%
11-Dec-2015	PPI Ex Food and Energy MoM	Nov	0.0%	0.1%	-0.3%
11-Dec-2015	Business Inventories	Oct	0.0%	0.1%	0.3%
11-Dec-2015	U. of Mich. Sentiment	Dec P	92.0	92.2	91.3

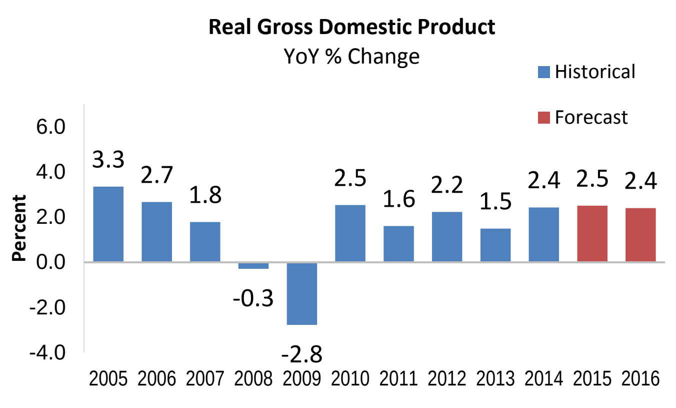
*Consensus from Bloomberg

What to Expect in 2016

2016 is right around-the-corner. I haven't even finished all my holiday shopping yet, and I am still working on Thanksgiving leftovers, but the New Year will be here before you know it. In this week's US Outlook Report, we give you a little preview of what you can expect from the U.S. economy and interest rates in 2016.

On the surface, we don't expect to see much of a change in the rate of overall U.S. economic growth. On a year-on-year basis, real GDP is expected to slow from 2.5% estimated for 2015 to 2.4% in 2016. The annual pace of growth in the U.S. has remained remarkably stable at around 2.4% to 2.5% since 2014.

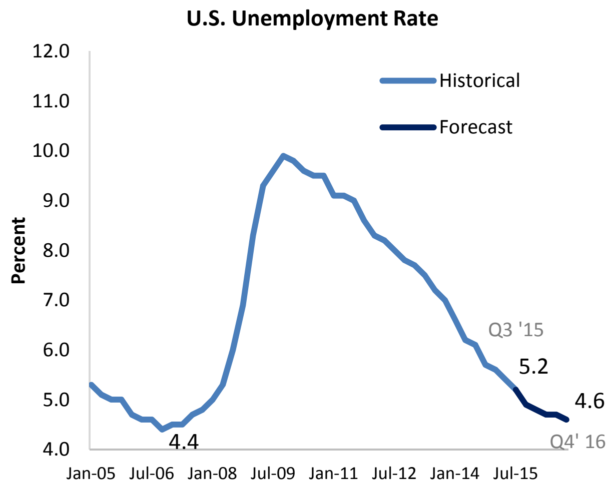
Stable and Respectable GDP Growth Continues in 2016



Source: Bureau of Economic Analysis; BOTW

The good news is this forecasted pace of real GDP growth is still faster than the U.S. economy's longer-term potential; given sluggish population growth, aging demographics, and lackluster productivity gains. As a result, you can expect a healthy labor market with unemployment rates that continue to decline, though perhaps at a somewhat slower rate than we have become accustomed over the past few years.

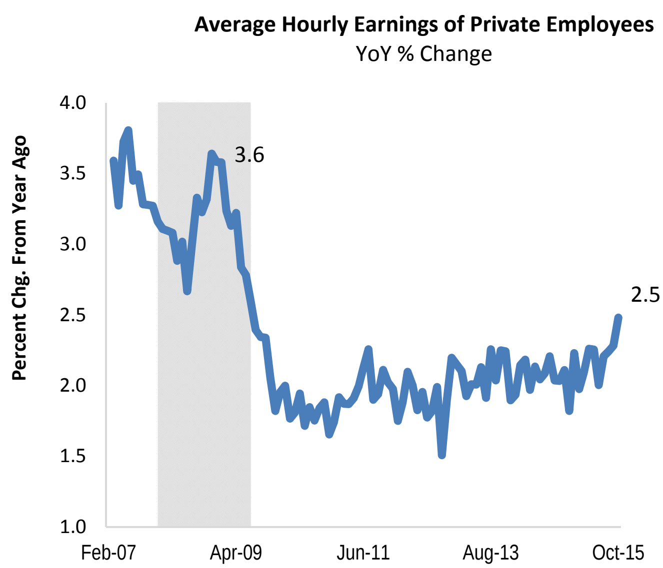
Finally A Sub-5.0% Unemployment Rate in the U.S.



Source: US. Bureau of Labor Statistics, Bank of the West Economics

As the U.S. unemployment rate falls next year below the U.S. economy's natural rate for the first time in a decade, nominal and real wages will rise at a faster clip. Average hourly earnings in last month's payroll report showed some encouraging signs of acceleration to around 2.5%. 2016 should see even faster average hourly earnings growth. An increase in average hourly earnings growth into the 3.0% range is entirely possible by the end of 2016.

Emerging Wage Pressures Will Become More Visible

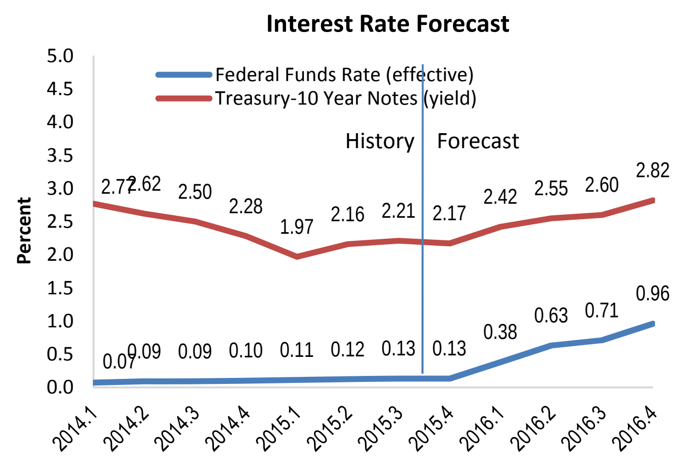


Source: Bureau of Labor Statistics

Already the Fed's Beige Book report for December noted: several Fed districts reported difficulties in finding skilled workers, lower-skilled and entry-level workers, as well as construction workers. The Cleveland, Atlanta, and San Francisco districts reported wage pressures were widespread or emerging. We expect these wage pressures to spread to more regions of the country as the U.S. unemployment rates continue to fall.

But the tranquil economic picture from GDP, employment, and wages masks a lot of shifts in the economic landscape, just beneath the surface, that could keep investors and some industries on edge. Top of mind will be the path of U.S. interest rate hikes from the Fed. Our baseline forecast is that the Federal Reserve will start raising interest rates this month, and three additional rate hikes will occur in 2016. Long-term interest rates, like mortgage rates, will rise as well, but their increases are expected to be more muted and should not kill off consumer spending, the housing recovery, or the stock market rebound.

Rising Interest Rates- Top of Mind For Investors in 2016



Source: Fed Reserve; BOTW Economics

Rising interest rates, if taken too far, do have the potential to have wide-ranging impacts on consumer spending, housing demand and construction, emerging market economies, commodity prices, and the U.S. dollar. Already we are seeing a divergent economic performance between manufacturers that are more exposed to the global slowdown and stronger dollar and service businesses that are more closely wedded to the strength of the U.S. consumer.

We will see this divergence continue into 2016. Expect more dollar appreciation, continued low oil prices, and pockets of strength and desperation across regions of the country and across industries. We expect to find relative strength in consumer spending and in the Coastal regions of the country and relative weakness in agriculture, business investment, manufacturing, and exports dampening economic activity in the middle of the country. Unfortunately not everyone will benefit from this two-speed economic expansion.

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*	-0.9	4.6	4.3	2.1	0.6	3.9	2.1	2.1	2.3	2.3	2.4	2.5	1.5	2.4	2.5	2.4
Personal Consumption Expenditures*	1.3	3.8	3.5	4.3	1.7	3.6	3.0	2.5	3.0	3.0	2.9	2.8	1.7	2.7	3.1	2.9
Non-residential Fixed Investment*	8.3	4.4	9.0	0.7	1.6	4.1	2.4	2.4	2.9	2.9	3.3	3.5	3.0	6.2	3.1	2.9
Private Housing Starts (000s units)	934	984	1,029	1,055	978	1,158	1,153	1,160	1,190	1,225	1,230	1,250	928	1,001	1,112	1,224
Vehicle Sales (mill. Units, annualized)	15.7	16.5	16.7	16.8	16.6	17.1	17.8	18.0	17.9	17.8	17.6	17.6	15.5	16.4	17.4	17.7
Industrial Production*	3.6	5.7	3.9	4.7	-0.3	-2.4	1.9	-0.1	1.8	1.9	1.9	1.8	1.9	3.7	1.4	1.2
Nonfarm Payroll Employment (mil.)	137.8	138.6	139.4	140.2	141.0	141.6	142.2	142.8	143.4	144.0	144.5	145.1	136.4	139.0	141.9	144.2
Unemployment rate	6.6	6.2	6.1	5.7	5.6	5.4	5.2	4.9	4.8	4.7	4.7	4.6	7.4	6.2	5.3	4.7
Consumer Price Index* (percent)	2.1	2.4	1.2	-0.9	-3.1	3.0	1.6	1.8	2.0	2.0	2.0	2.1	1.5	1.6	0.2	2.0
"Core" CPI* (percent)	1.8	2.2	1.4	1.5	1.7	2.5	1.7	1.5	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	-11.2	3.6	0.8	-4.0	1.7	1.7	1.8	1.8	1.2	1.9	-3.1	0.6
Trade Weighted Dollar (Fed BOG, major)	76.9	76.4	77.5	82.5	89.3	90.0	91.7	93.0	95.2	96.4	97.5	98.7	75.9	78.4	91.0	97.0
Crude Oil Prices -WTI ($ per barrel)	99	103	98	73	48	58	47	45	47	49	51	51	98	93	50	50

*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	2009	2,064	2102	2027						1,644	1,930		
Dow Jones Industrial Average	16,177	16,604	16,954	17345	17,808	18,004	17,077						15,010	16,770		
Federal Funds Rate (effective)	0.07	0.09	0.09	0.10	0.11	0.12	0.13	0.13	0.38	0.63	0.71	0.96	0.11	0.09	0.13	0.67
Treasury-3 Month Bills (yield)	0.05	0.03	0.03	0.02	0.02	0.02	0.09	0.09	0.32	0.57	0.65	0.90	0.06	0.03	0.06	0.61
Treasury-2 Year Notes (yield)	0.37	0.42	0.52	0.54	0.60	0.61	0.68	0.75	1.07	1.36	1.47	1.73	0.31	0.46	0.66	1.41
Treasury-5 Year Notes (yield)	1.60	1.66	1.70	1.60	1.46	1.53	1.55	1.55	1.82	2.02	2.17	2.30	1.17	1.64	1.52	2.08
Treasury-10 Year Notes (yield)	2.77	2.62	2.50	2.28	1.97	2.16	2.21	2.17	2.42	2.55	2.60	2.82	2.35	2.54	2.13	2.60
Treasury-30 Year Notes (yield)	3.68	3.44	3.27	2.97	2.55	2.88	2.96	2.95	3.08	3.14	3.23	3.36	3.44	3.34	2.84	3.20
Prime Rate	3.25	3.25	3.25	3.25	3.25	3.25	3.25	3.25	3.50	3.75	3.83	4.08	3.25	3.25	3.25	3.79
Libor 3-Mo. U.S. Dollar	0.26	0.25	0.24	0.25	0.30	0.30	0.31	0.36	0.57	0.82	0.90	1.15	0.28	0.25	0.32	0.86
Mortgage-30 Year (yield)	4.36	4.23	4.14	3.96	3.72	3.82	3.95	3.86	4.11	4.24	4.31	4.54	3.98	4.17	3.84	4.30
BAA Corporate (yield)	5.12	4.82	4.74	4.73	4.50	4.83	5.24	5.40	5.54	5.69	5.79	6.03	5.10	4.86	4.99	5.76

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