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# U.S. & California Economic Outlook: What's Ahead for 2014

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March 5, 2014

Together we'll go far



### Less Uncertainty

- Deals on the federal budget and debt ceiling, along with the uneventful start of Fed tapering have removed some of the uncertainty hanging over the economy.

### Slower Growth in the Near-term

- Despite stronger GDP growth during the second half of 2013, we expect economic growth to slow during the first half of 2014 and remain below its long-run trend. Expectations have been reset lower.

### Unconventional Monetary Policy

- QE has boosted asset prices more than it has the economy's underlying fundamentals. Income and wealth inequality remain potent issues.

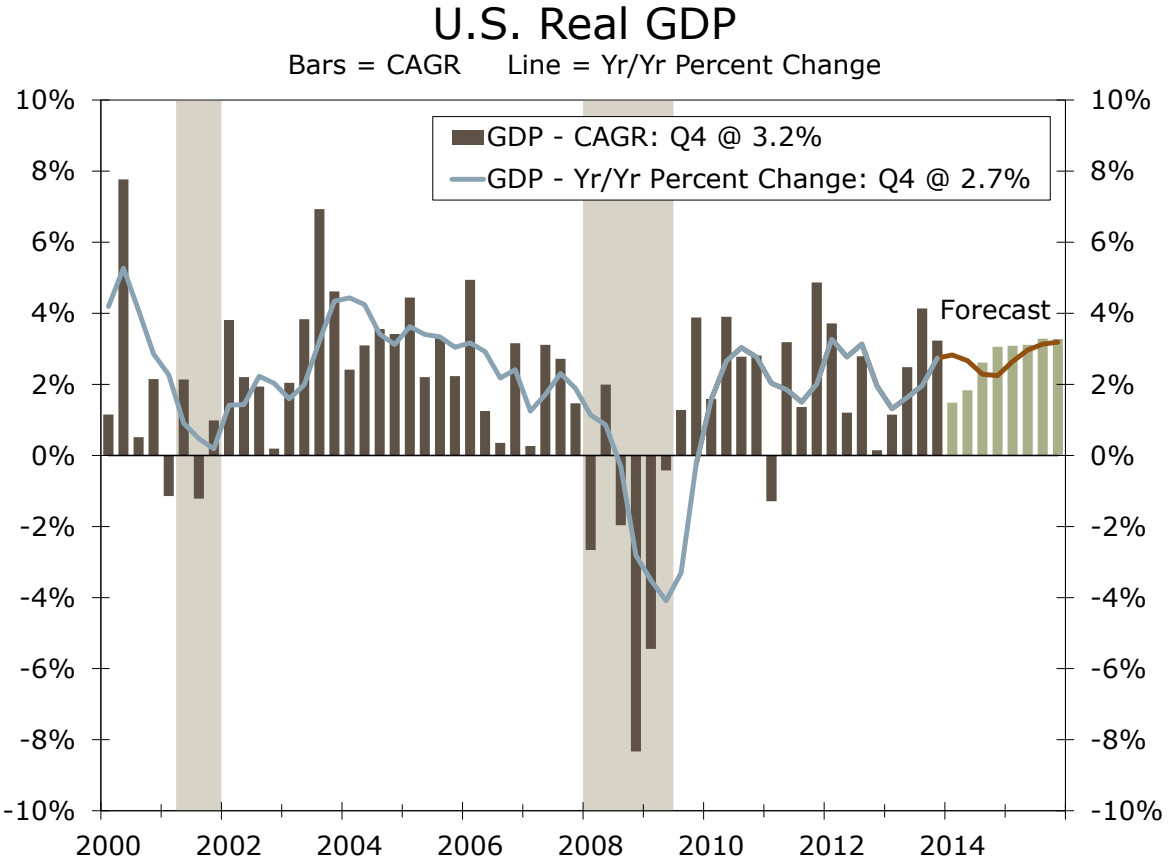
### Global Economy

- Despite rumblings in some developing economies, the global economic outlook remains positive, with global growth expected to improve in 2014.

### Growth is Uneven

- Energy and technology have been two notable bright spots in this otherwise disappointing economic recovery.

After a surprisingly strong second half of 2013, real GDP growth will likely decelerate during the first half of 2014.



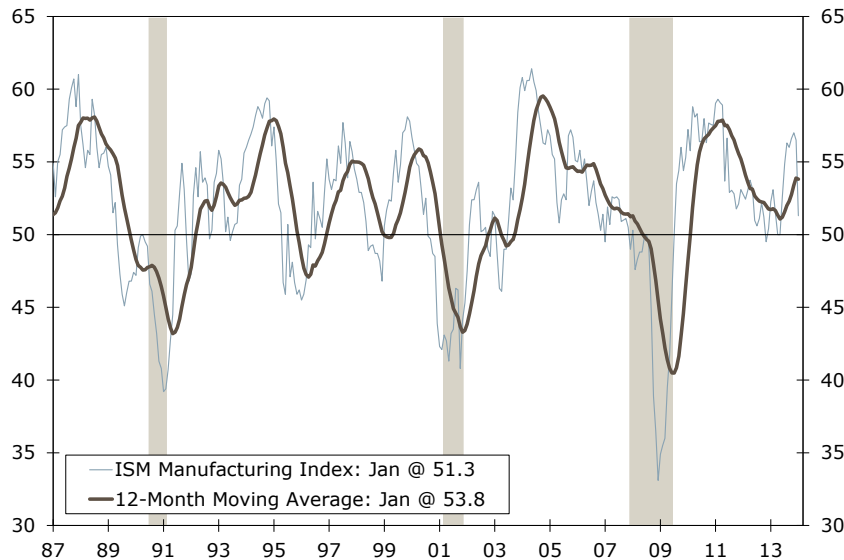
Source: U.S. Department of Commerce and Wells Fargo Securities, LLC

Manufacturing activity is cooling off as business strive to reduce inventories.

## ISM

### ISM Manufacturing Composite Index

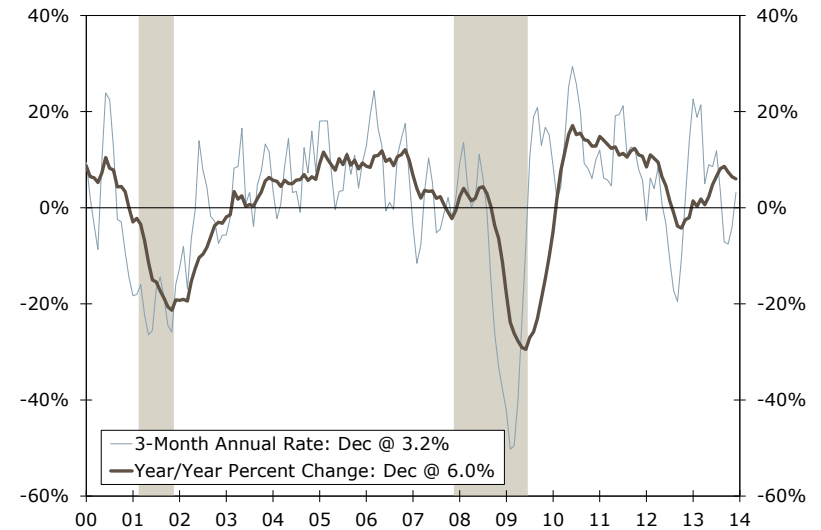
Diffusion Index



## Capital Goods Orders

### Nondefense Capital Goods Orders, Ex-Aircraft

Seasonally Adjusted, 3-Month Moving Averages



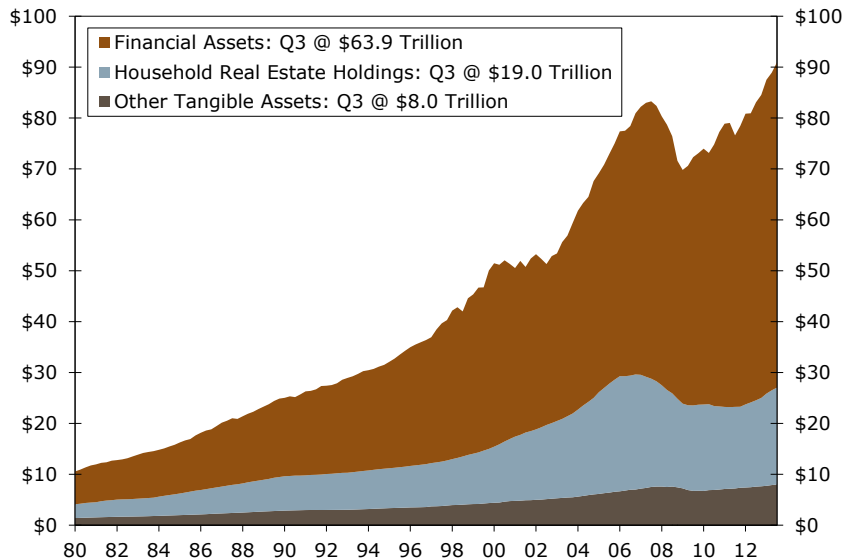
Source: ISM, Census and Wells Fargo Securities, LLC

Rising stock prices have helped bolster household finances at a time when real incomes are barely growing. Rising asset prices have helped bolster economic activity at the upper end. Conditions for the vast middle remain bogged down by sluggish wage and salary growth.

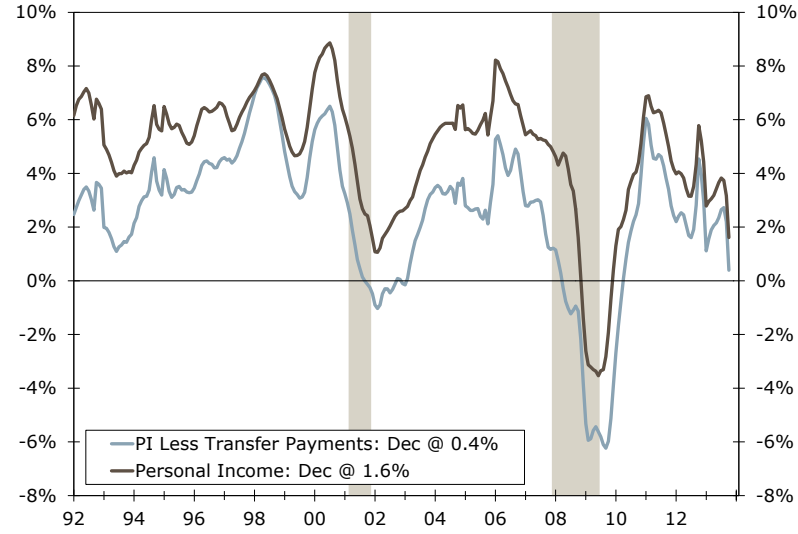
**Household Wealth**

**Personal Income**

**Household Assets**  
Trillions of Dollars

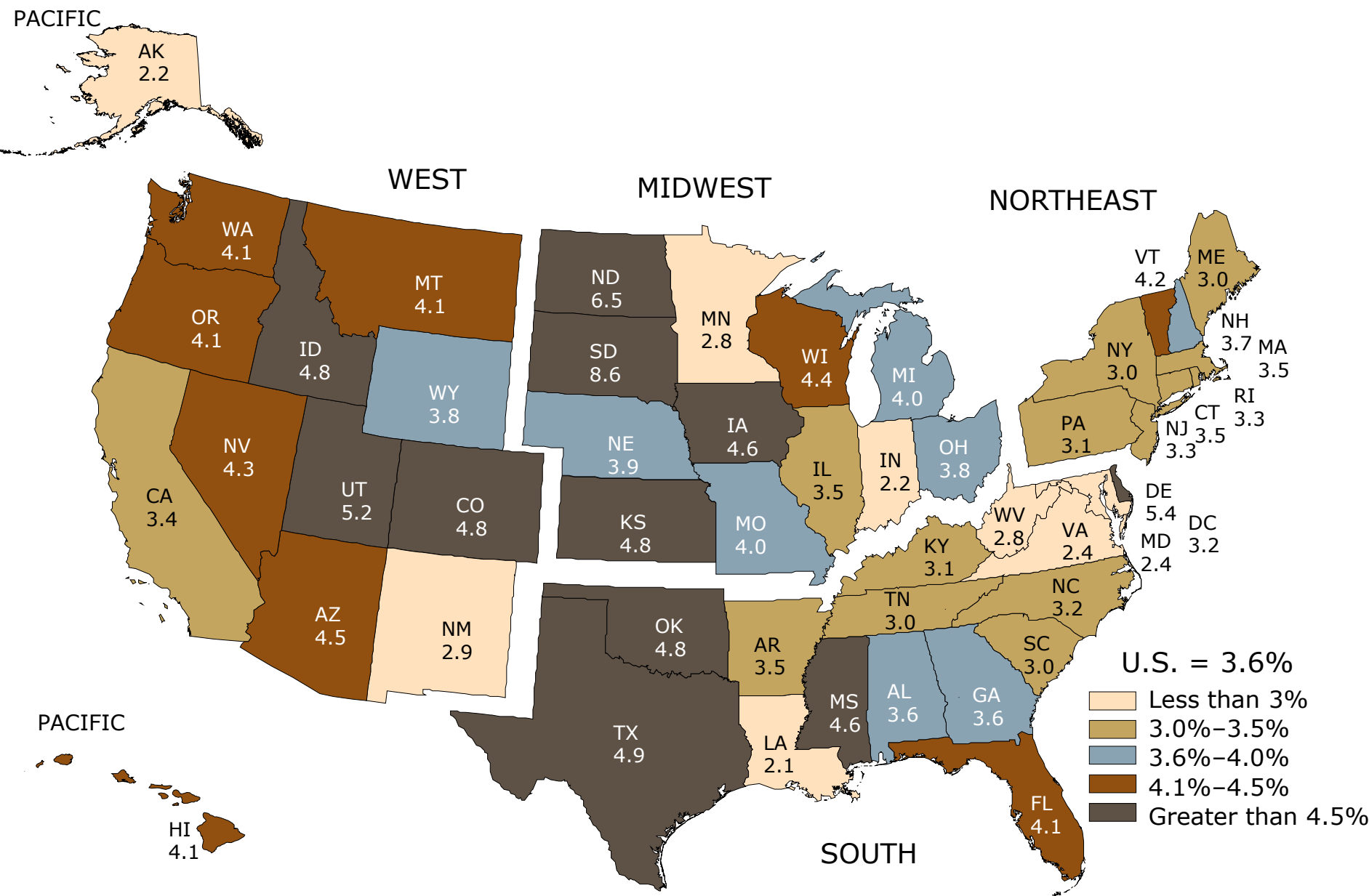


**PI vs. PI Less Transfer Payments**  
Year-over-Year Percent Change, 3-Month Moving Average



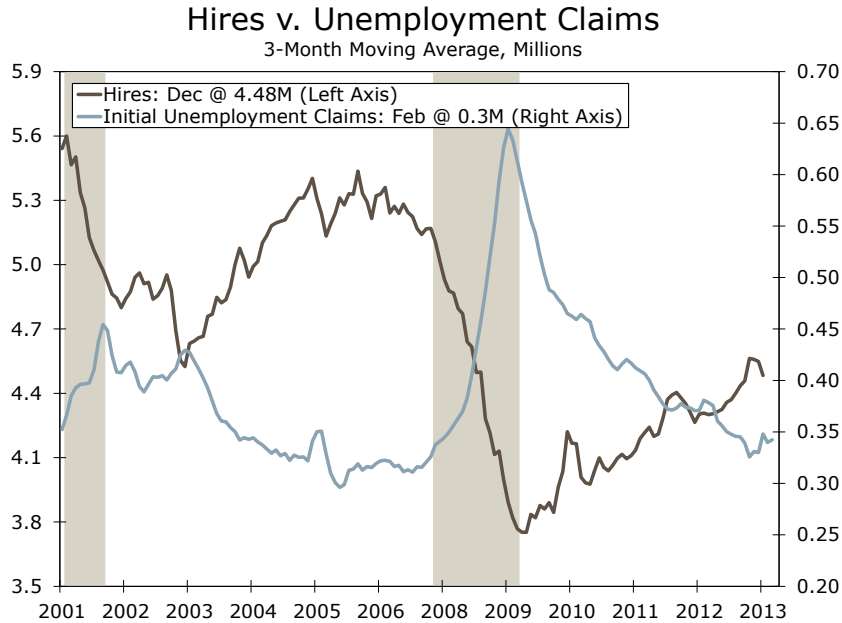
Source: U.S. Department of Commerce, Conference Board and Wells Fargo Securities, LLC

# Percent change in Personal Income Q3 2012-Q3 2013

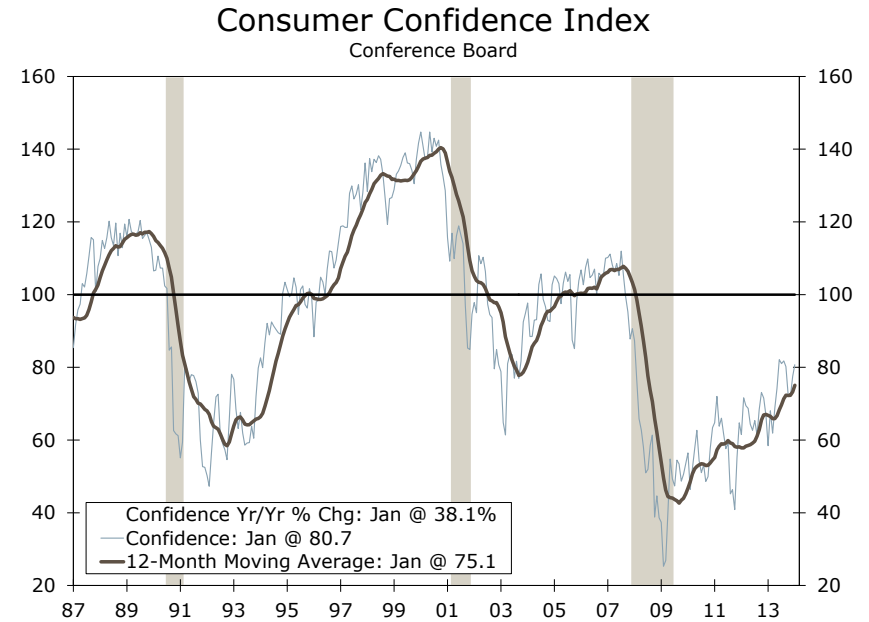


Job growth holds the key to improvements in consumer confidence.

Hires v. Unemployment Claims



Consumer Confidence

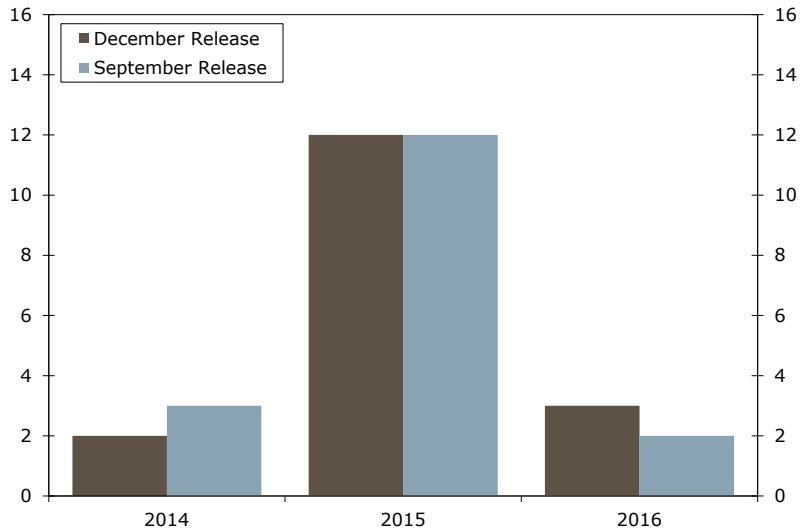


Source: Conference Board, U.S. Department of Commerce and Wells Fargo Securities, LLC

Most FOMC members currently expect short-term interest rates to remain on hold until 2015. We expect Fed communications on interest rate policy to shift over the course of this year.

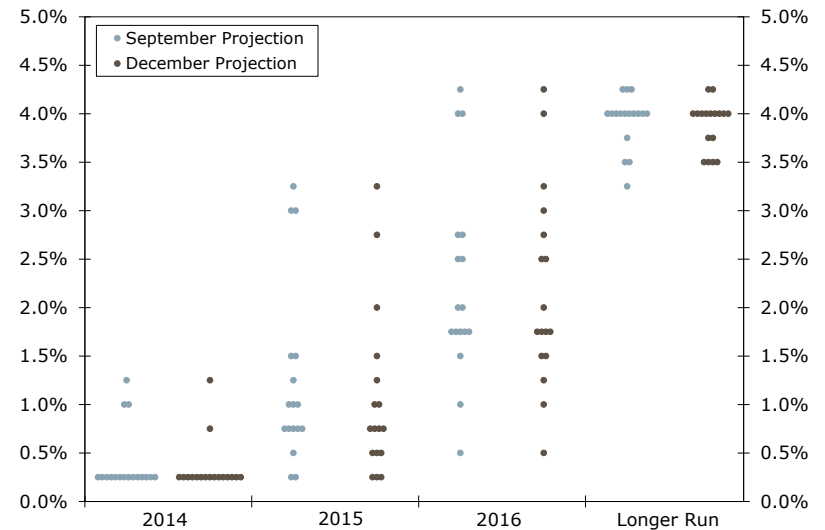
### Timing of Firming

Appropriate Timing of Policy Firming  
Number of Participants



### Target Fed Funds Rate

Appropriate Pace of Policy Firming  
Target Federal Funds Rate at Year-End

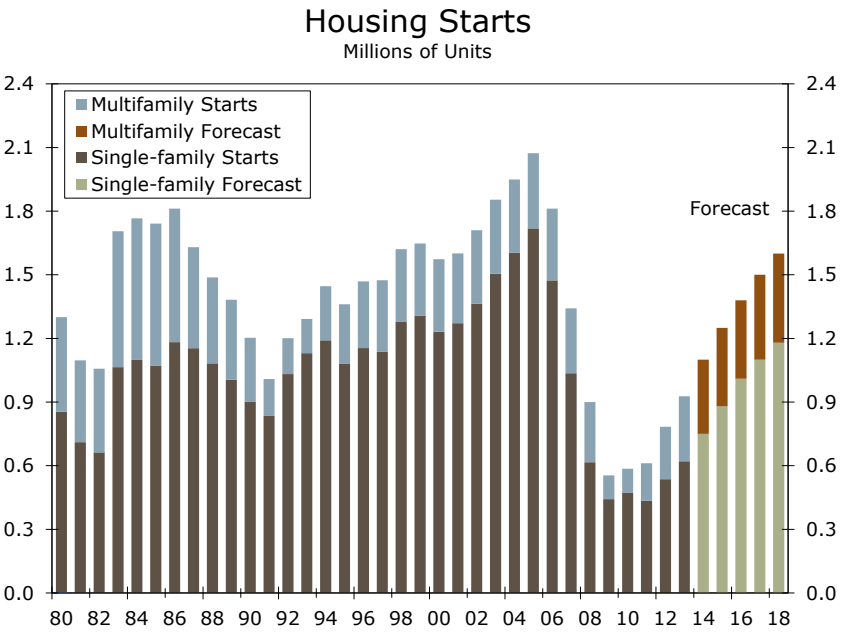


Source: Federal Reserve Board and Wells Fargo Securities, LLC

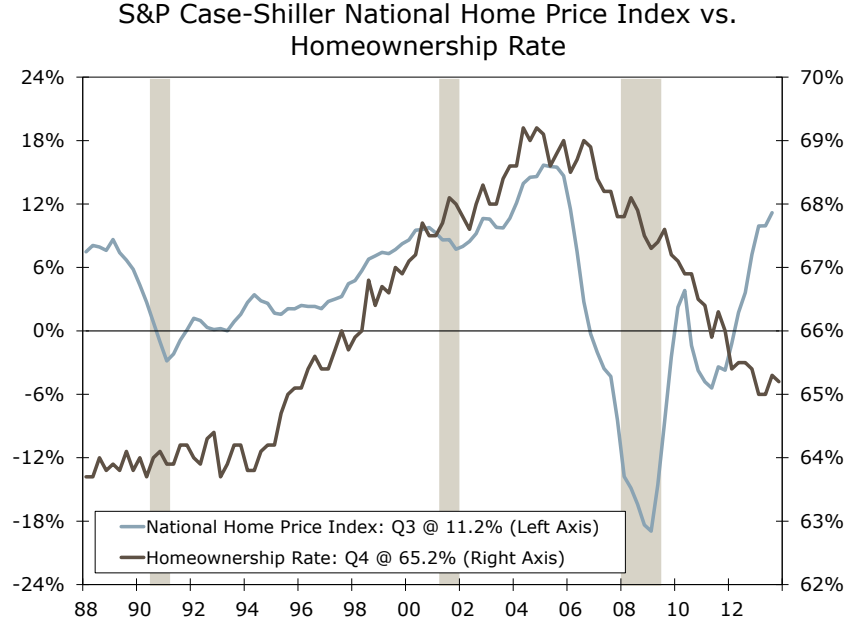


Despite some recent setbacks, we continue to look for a gradual recovery in homebuilding. Apartments are playing a larger role than in previous building cycles.

## Housing Starts



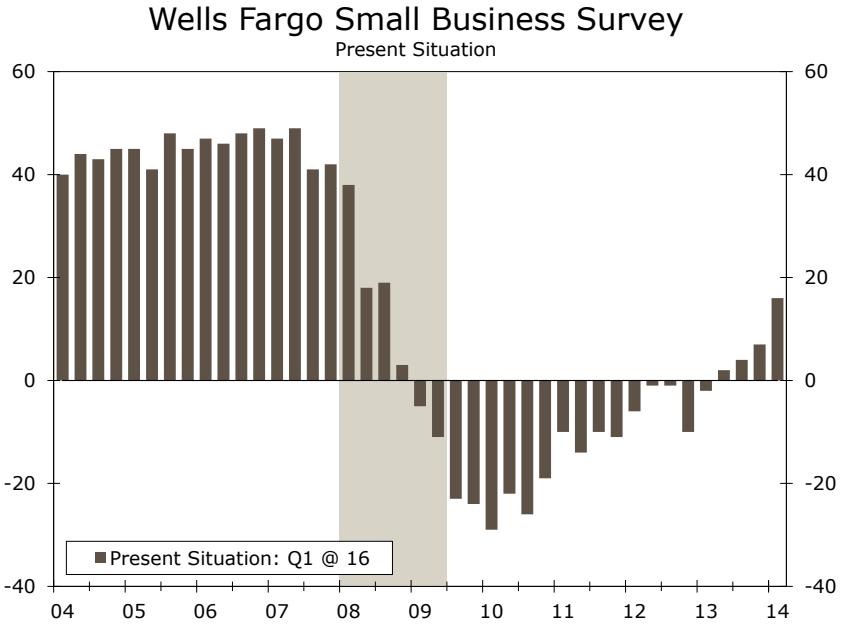
## Home Prices



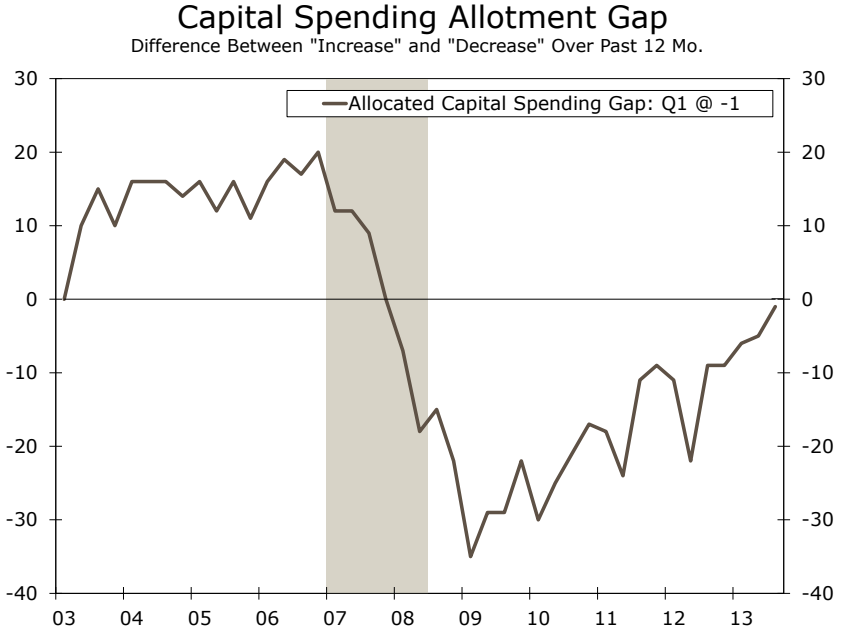
Source: U.S. Department of Commerce, CoreLogic Case Shiller and Wells Fargo Securities, LLC

Small businesses remain cautious but recent surveys show some improvement. View on capital spending and hiring continue to gradually trend higher.

Small Business Confidence



Capital Spending Gap



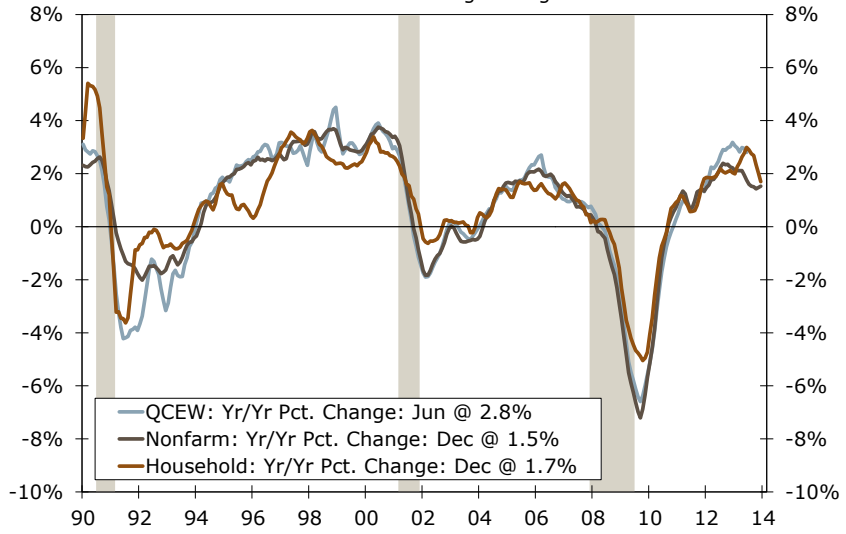
Source: Gallup, Wells Fargo Bank and Wells Fargo Securities, LLC

Employment gains have been heavily weighted toward the state's larger metropolitan areas along the coast.

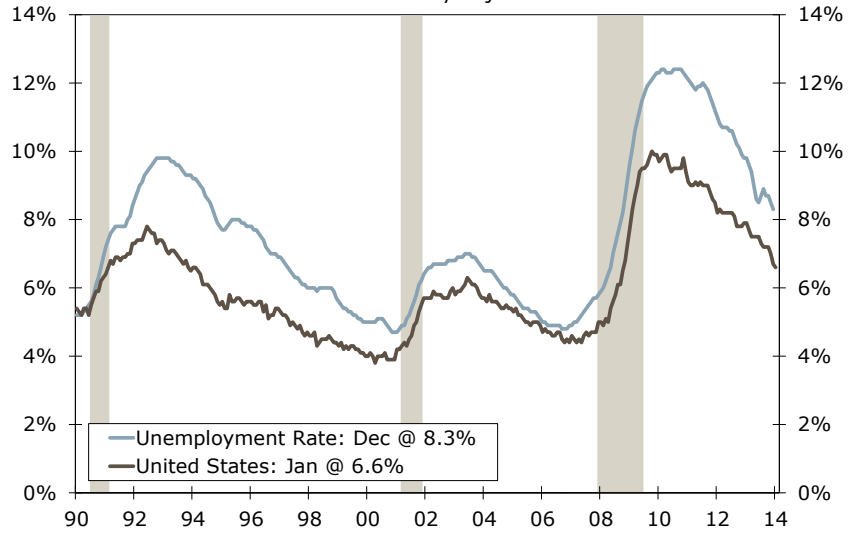
**Employment**

**Unemployment**

California Nonfarm Employment  
3-Month Moving Averages



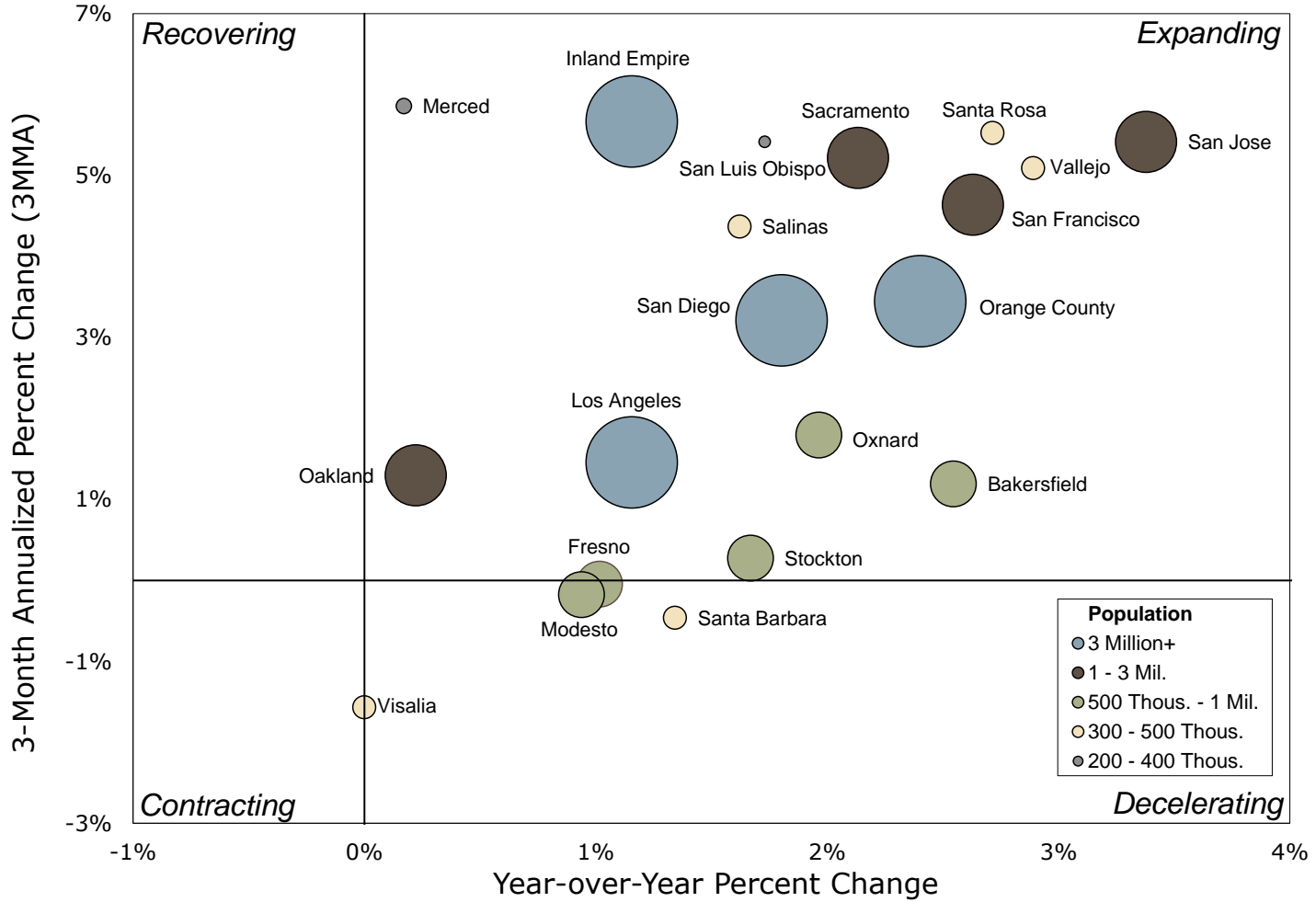
California vs. U.S. Unemployment Rate  
Seasonally Adjusted



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

# California Employment Growth: December 2013

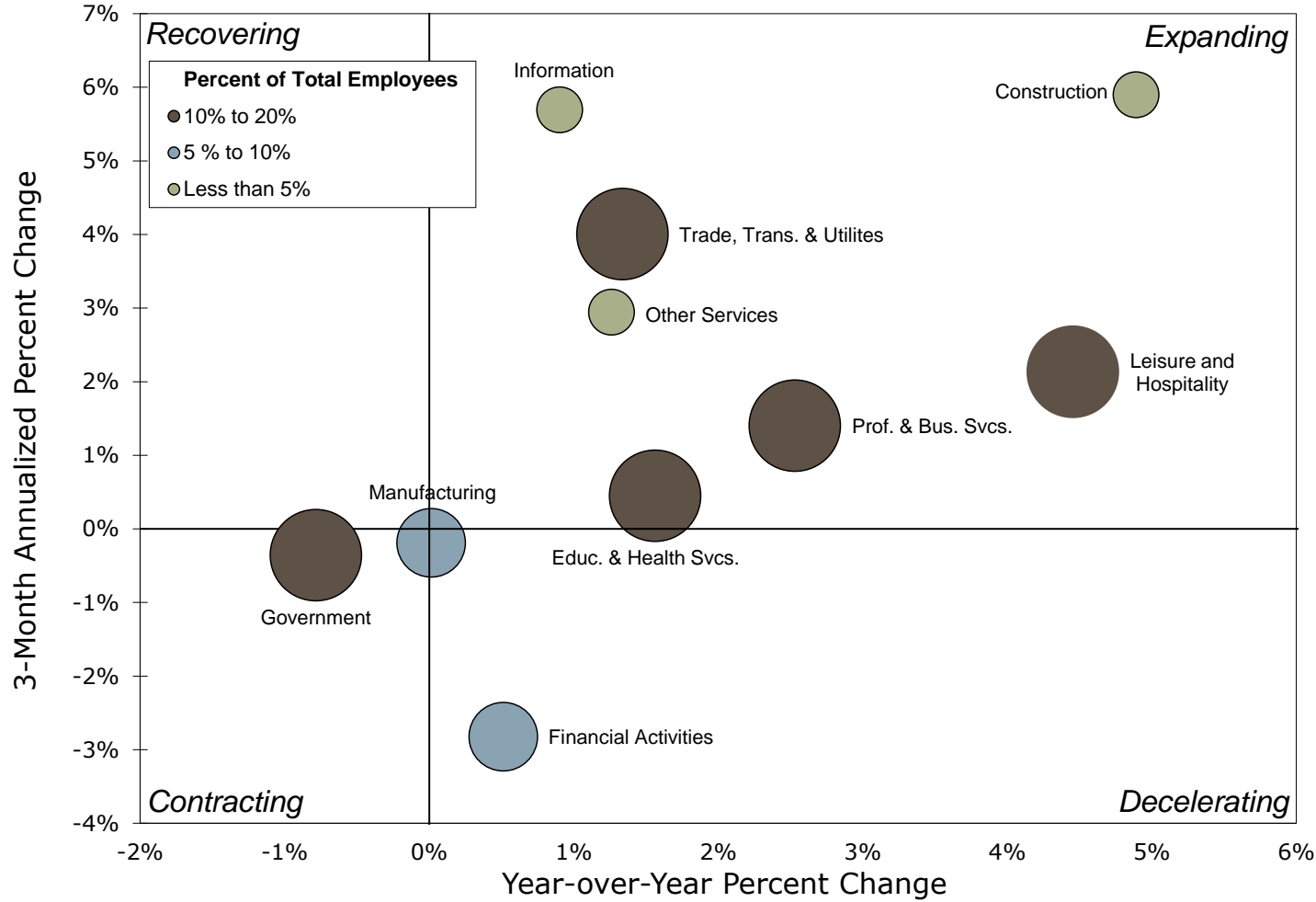
## 3-Month Moving Averages



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

# California Employment Growth by Industry

3-Month Moving Averages, December 2013

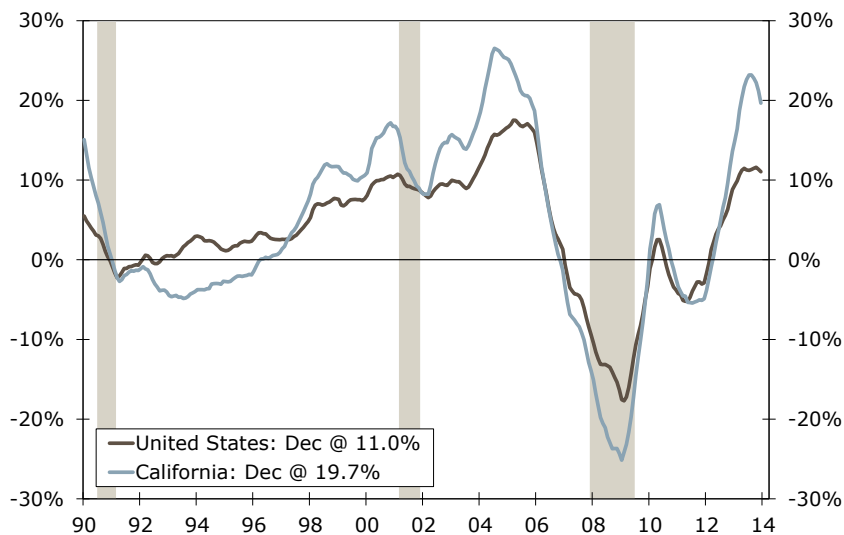


Source: U.S. Department of Labor and Wells Fargo Securities, LLC

The housing market is improving but still remains well below prerecession levels.

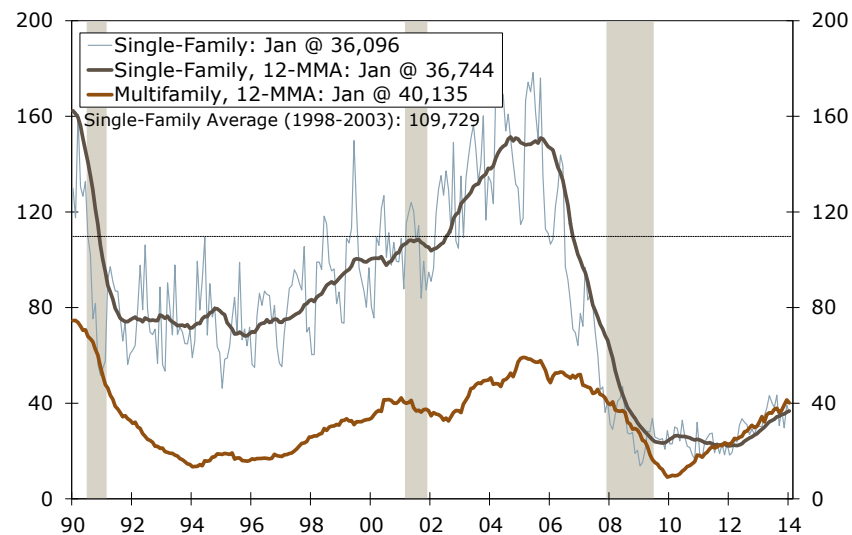
### Home Prices

Core Logic HPI: CA vs. U.S.  
Year-over-Year Percent Change



### Housing Permits

California Housing Permits  
Thousands of Permits, Seasonally Adjusted Annual Rate



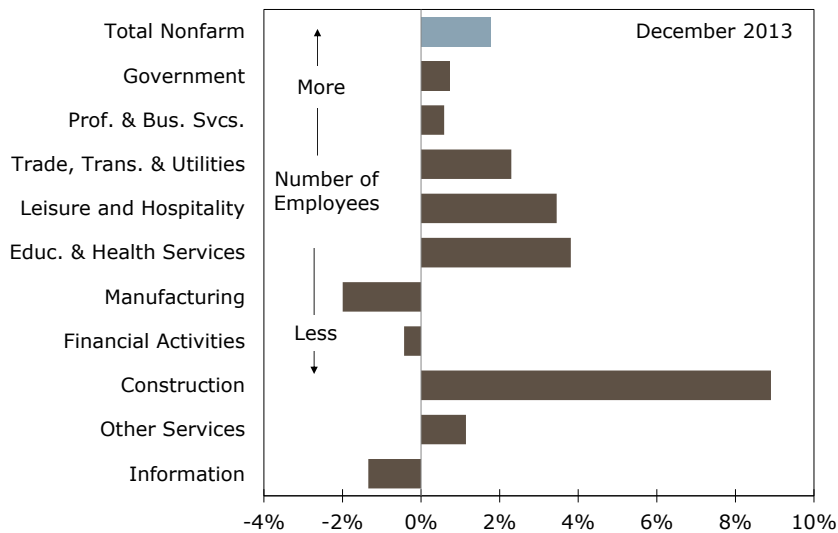
Source: U.S. Department of Commerce and Wells Fargo Securities, LLC

San Diego has seen broad based employment gains across most sectors.

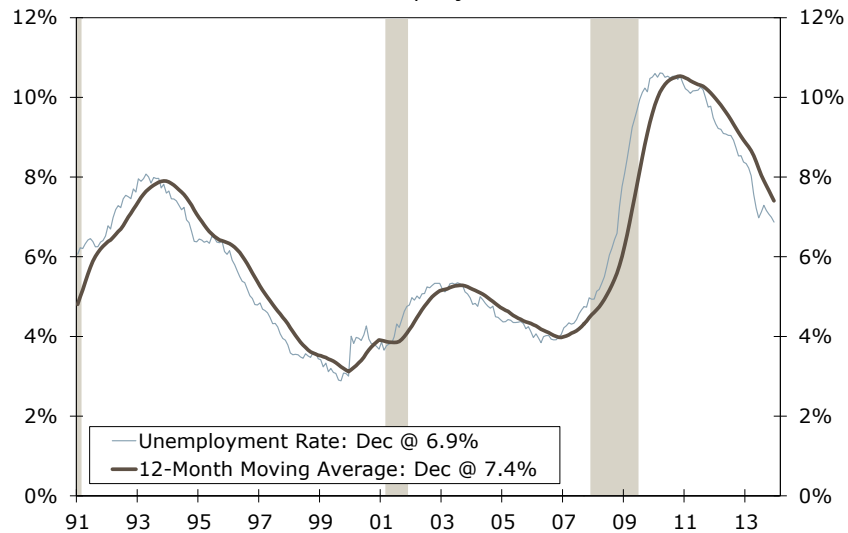
**Employment**

**Unemployment**

San Diego MSA Employment Growth By Industry  
Year-over-Year Percent Change, 3-MMA



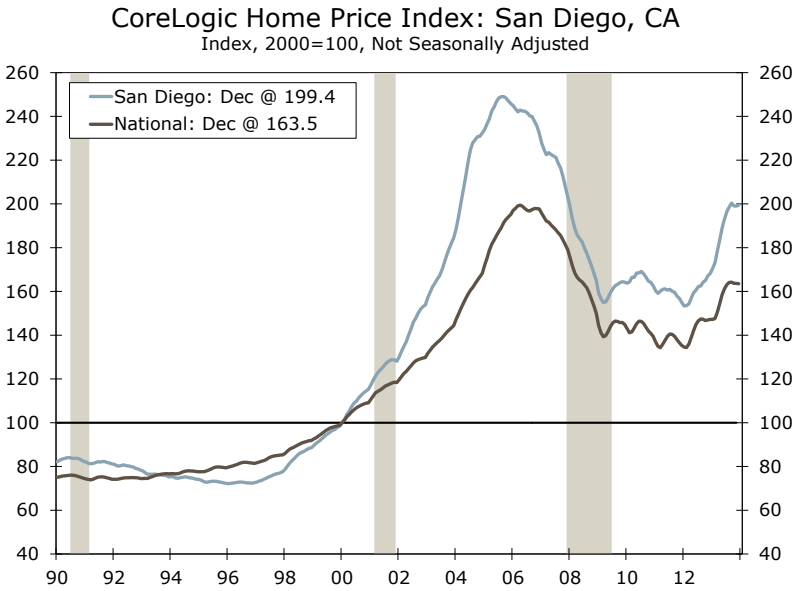
San Diego MSA Unemployment Rate  
Seasonally Adjusted



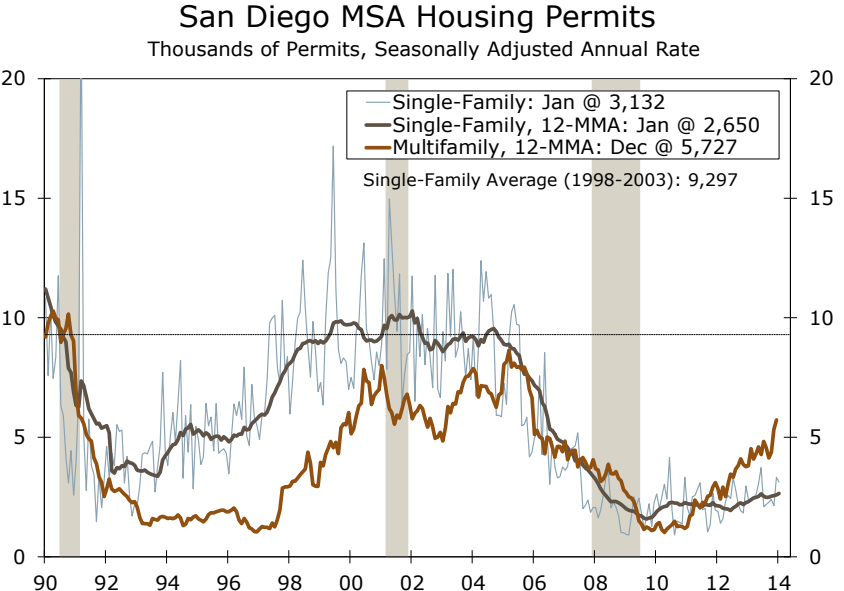
Source: U.S. Department of Commerce and Wells Fargo Securities, LLC

Home prices in San Diego have recovered and are now at levels seen prior to the recession

### Home Price Index



### Housing Permits



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

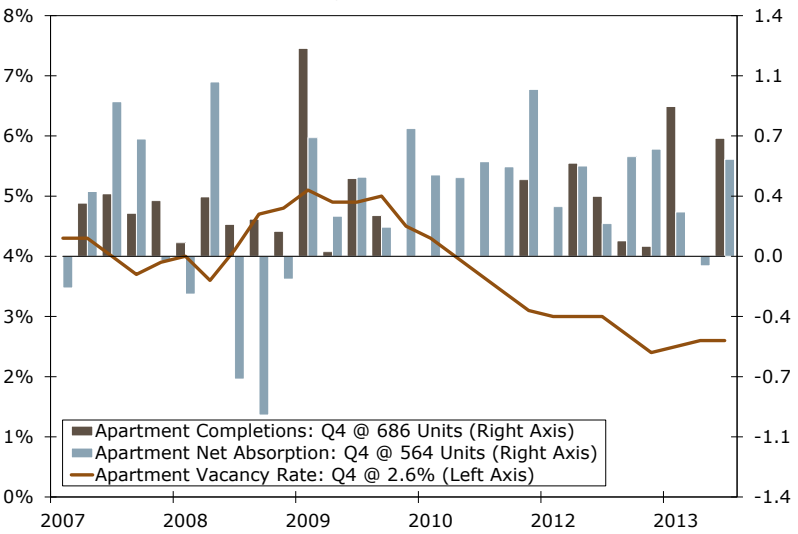


Growth has been seen in the San Diego apartment market.

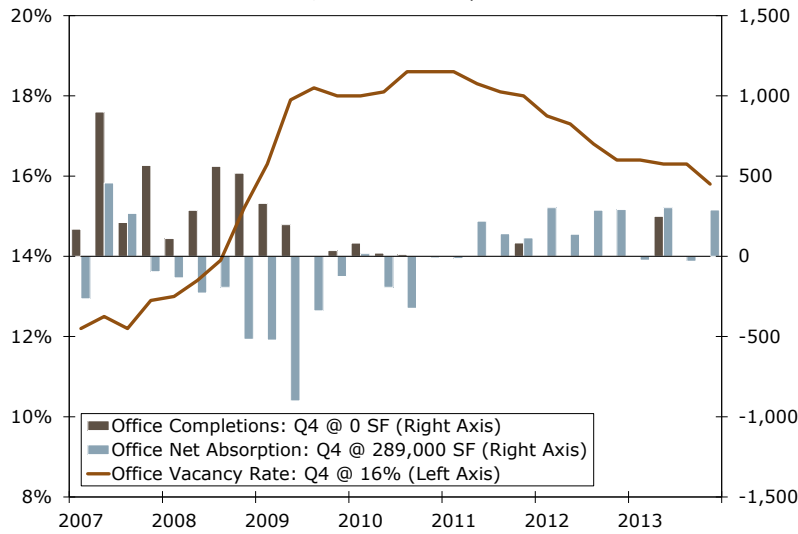
Apartment

Office

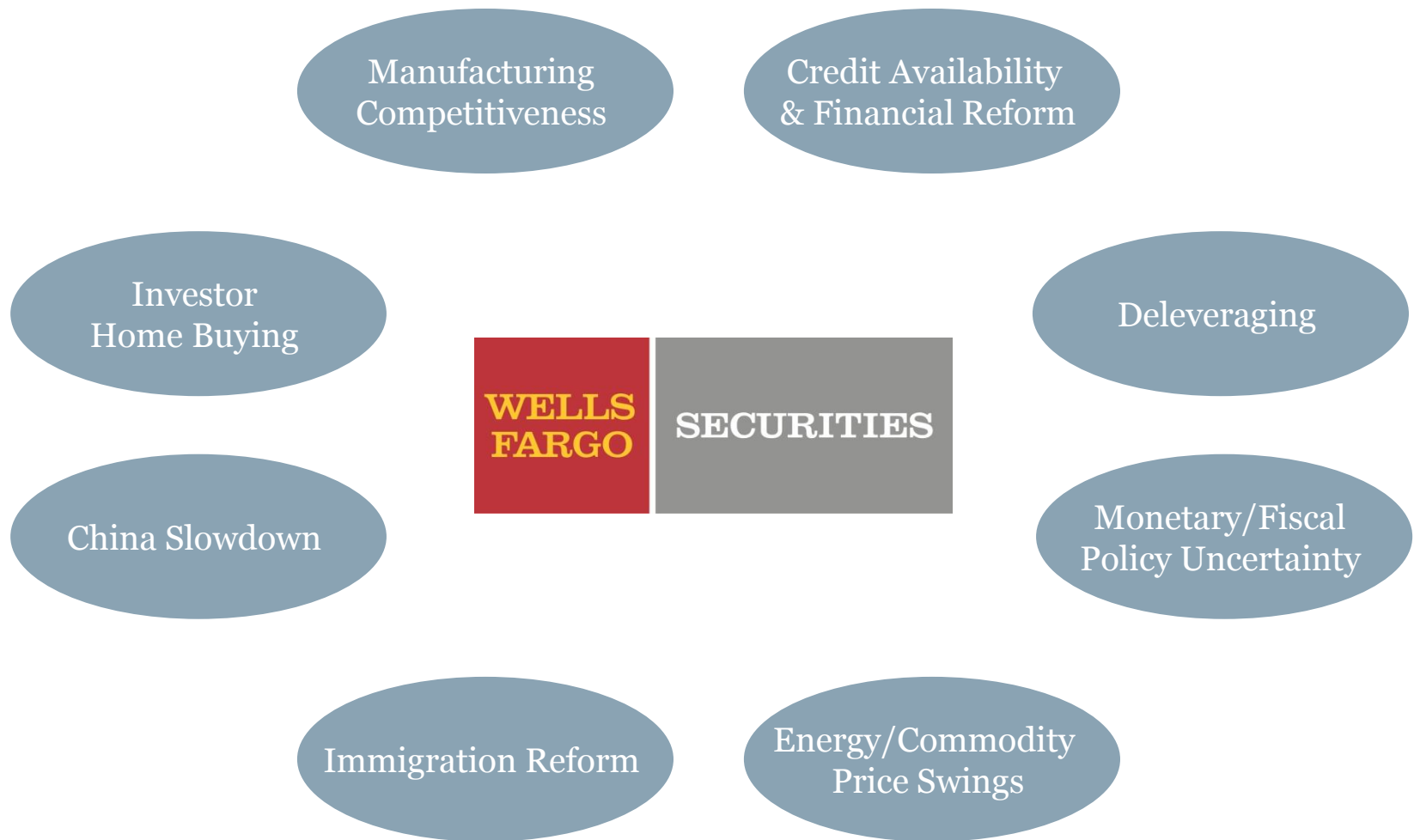
San Diego Apartment Supply & Demand  
Percent, Thousands of Units



San Diego Office Supply & Demand  
Percent, Thousands of Square Feet



Source: REIS and Wells Fargo Securities, LLC



## Wells Fargo U.S. Economic Forecast

	Actual				Forecast				Actual			Forecast	
	2013				2014				2011	2012	2013	2014	2015
	1Q	2Q	3Q	4Q	1Q	2Q	3Q	4Q					
Real Gross Domestic Product <sup>1</sup>	1.1	2.5	4.1	3.2	1.5	1.8	2.6	3.1	1.8	2.8	1.9	2.5	3.0
Personal Consumption	2.3	1.8	2.0	3.3	2.9	2.2	2.2	2.3	2.5	2.2	2.0	2.5	2.5
Inflation Indicators <sup>2</sup>													
PCE Deflator	1.4	1.1	1.1	0.9	1.1	1.6	1.6	2.0	2.4	1.8	1.1	1.6	2.2
Consumer Price Index	1.7	1.4	1.6	1.2	1.4	1.9	1.7	2.0	3.1	2.1	1.5	1.8	2.1
Industrial Production <sup>1</sup>	4.1	1.2	2.4	6.8	4.9	4.3	4.4	4.5	3.4	3.6	2.6	4.5	4.7
Corporate Profits Before Taxes <sup>2</sup>	2.1	4.5	5.7	5.0	4.1	5.4	5.5	5.6	7.9	7.0	4.3	5.2	5.9
Trade Weighted Dollar Index <sup>3</sup>	76.2	77.5	75.2	76.4	77.8	78.5	79.5	80.0	70.9	73.5	75.9	78.9	80.6
Unemployment Rate	7.7	7.5	7.2	7.0	6.5	6.5	6.4	6.4	8.9	8.1	7.4	6.5	6.2
Housing Starts <sup>4</sup>	0.96	0.87	0.88	1.00	0.99	1.04	1.10	1.16	0.61	0.78	0.92	1.07	1.22
Quarter-End Interest Rates <sup>5</sup>													
Federal Funds Target Rate	0.25	0.25	0.25	0.25	0.25	0.25	0.25	0.25	0.25	0.25	0.25	0.25	0.44
Conventional Mortgage Rate	3.57	4.07	4.49	4.46	4.60	4.76	4.83	4.98	4.46	3.66	3.98	4.79	5.23
10 Year Note	1.87	2.52	2.64	3.04	3.05	3.18	3.34	3.47	2.78	1.80	2.35	3.26	3.66

Forecast as of: February 12, 2014

<sup>1</sup> Compound Annual Growth Rate Quarter-over-Quarter

<sup>2</sup> Year-over-Year Percentage Change

<sup>3</sup> Federal Reserve Major Currency Index, 1973=100 - Quarter End

<sup>4</sup> Millions of Units

<sup>5</sup> Annual Numbers Represent Averages

# Appendix

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## A Sampling of Our Recent Special, Regional &amp; Industry Commentary

## Recent Special Commentary

Date	Title	Authors
February-13	Should Developing Economies Worry Us? Part II	Bryson, Alemán & Griffiths
February-10	Inflation Chartbook: February 2014	Bullard & House
February-07	Natural Gas Prices Pose Only Small Challenge to Consumers	House & Brown
February-05	What's Next for Argentina After the Devaluation?	Aleman
February-05	Brazilian Industrial Production Took a Nosedive in December	Aleman
February-03	Charlotte Metro Area: A Delicate Balance	Silvia & Brown
February-03	The Russian Economy Slows Down Considerable in 2013	Aleman
January-29	California's Recovery Remains Solidly On Track	Vitner & Wolf
January-29	FOMC: Improving Economy, Low Inflation, Tapering Persists	Silvia
January-29	Should Developing Economies Worry Us?	Bryson
January-29	Florida's Economy Continues to Heat Up	Vitner & Miller
January-29	Taiwan Enjoyed Modest, But Broad-Based, Growth in Q4	Bryson
January-28	Texas Keeps on Truckin'	Vitner & Wolf
January-28	British Economy Continues to Post Solid Growth	Bryson
January-27	Is the European Sovereign Debt Crisis Solved?	Bryson & Miller
January-27	Mexican Economy Continued to Struggle Late in 2013	Aleman
January-24	Argentina Is in the News Again	Aleman
January-24	Are U.K. Rate Hikes in the Cards?	Bryson
January-23	The "Unsustainable" Path of Federal Fiscal Policy: Part IV	Silvia & Brown
January-21	Slower Growth in China Here to Stay	Bryson
January-17	The Brazilian Central Bank Pushes Forward	Aleman
January-16	Is Slower Health Care Hiring Here to Stay?	Silvia, House & Silverman
January-16	Birmingham's Recovery Appears to Be Restarting	Vitner & Wolf
January-13	Mexican Industrial Production Disappoints Again	Aleman
January-10	Will The European Central Bank Ease Further?	Bryson
January-07	Housing Data Wrap-Up: December 2013	Vitner, Khan & Silverman
January-06	Another Debt Ceiling Deadline	Silvia & Brown
January-02	Singapore GDP Fell in Q4, But Underlying Trend is Solid	Bryson
January-02	Argentine Economy Remains Strong in Q3	Aleman
December-31	Colorado 2014 Economic Outlook	Vitner & Silverman
December-31	The Labor Market and Credit Risk	Silvia, Iqbal & Zachary
December-24	North Carolina's Unemployment Rate Tumbles in November	Vitner
December-24	Texas: Frequently Asked Questions	Vitner & Wolf
December-24	Our Favorite Charts of 2013	
December-20	Hotel Demand Remains Solid, but Cooling Is Expected	Khan, Zachary & Miller
December-20	California Posts Another Big Job Gain in November	Vitner
December-20	Florida's Jobless Rate Falls to 6.4 Percent in November	Vitner & Silverman
December-20	Georgia 2014 Economic Outlook	Vitner & Silverman
December-18	FOMC: Improving Economy, Low Inflation, Tapering to Start	Silvia & House
December-18	Pennsylvania: Five Issues for 2014	Vitner & Wolf

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