

WELLS
FARGO

SECURITIES

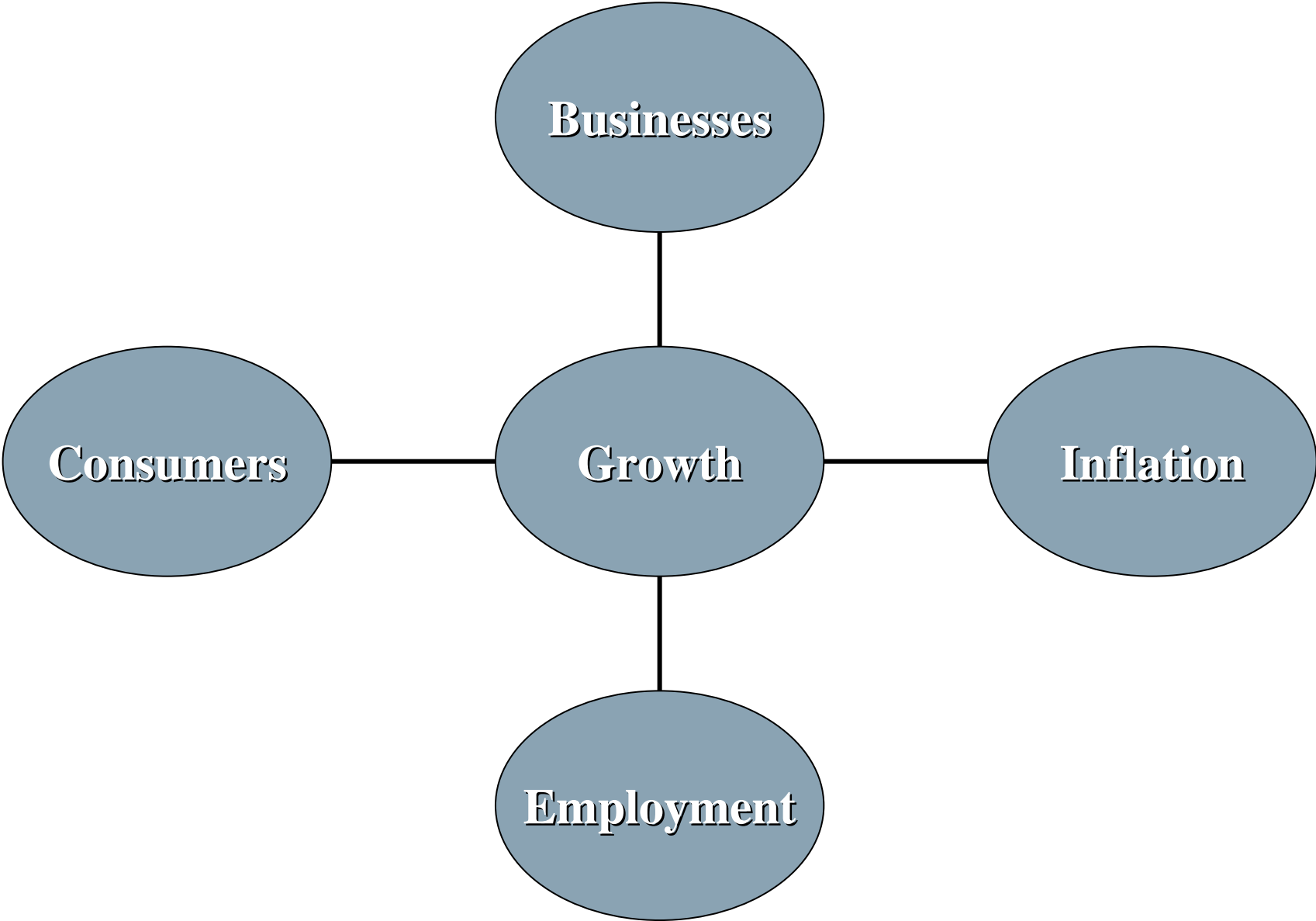
Economic Outlook for 2012 and Beyond

Michael A. Brown, Economist

February 14, 2012

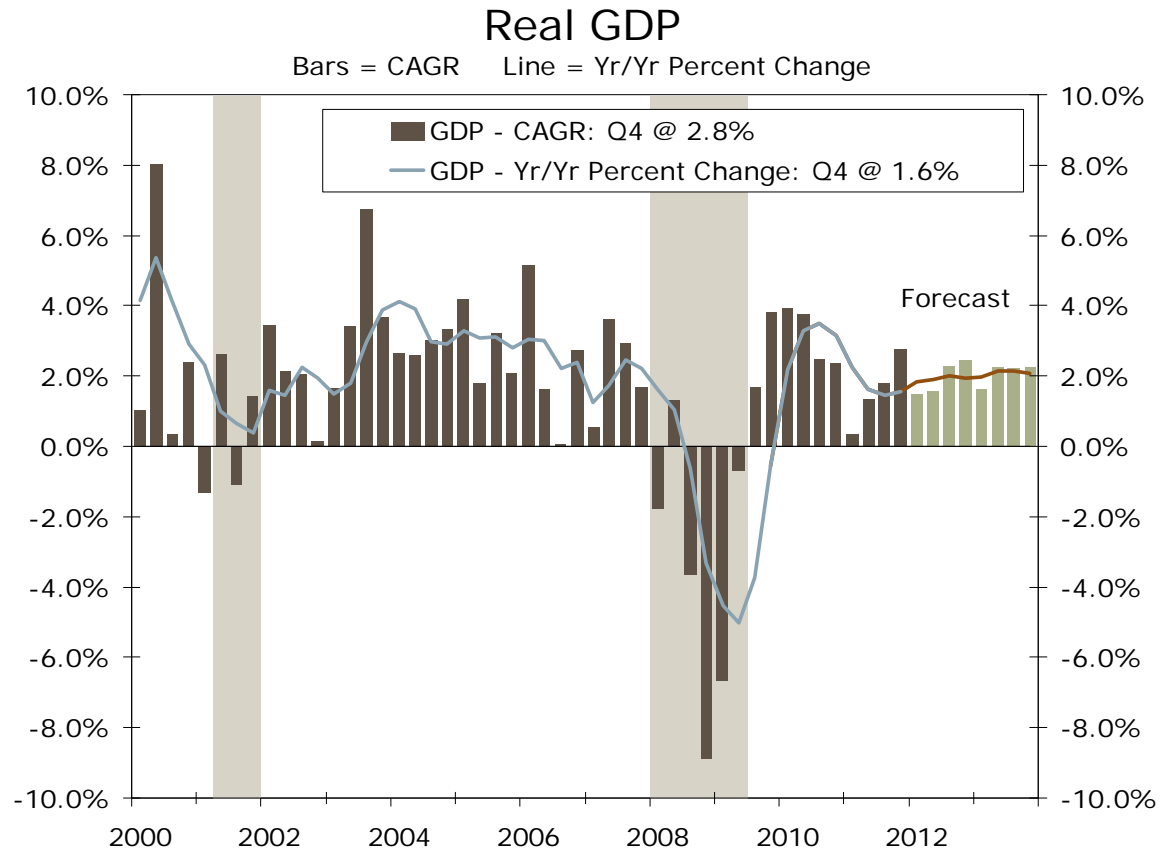
Together we'll go far





Where Are We Now?

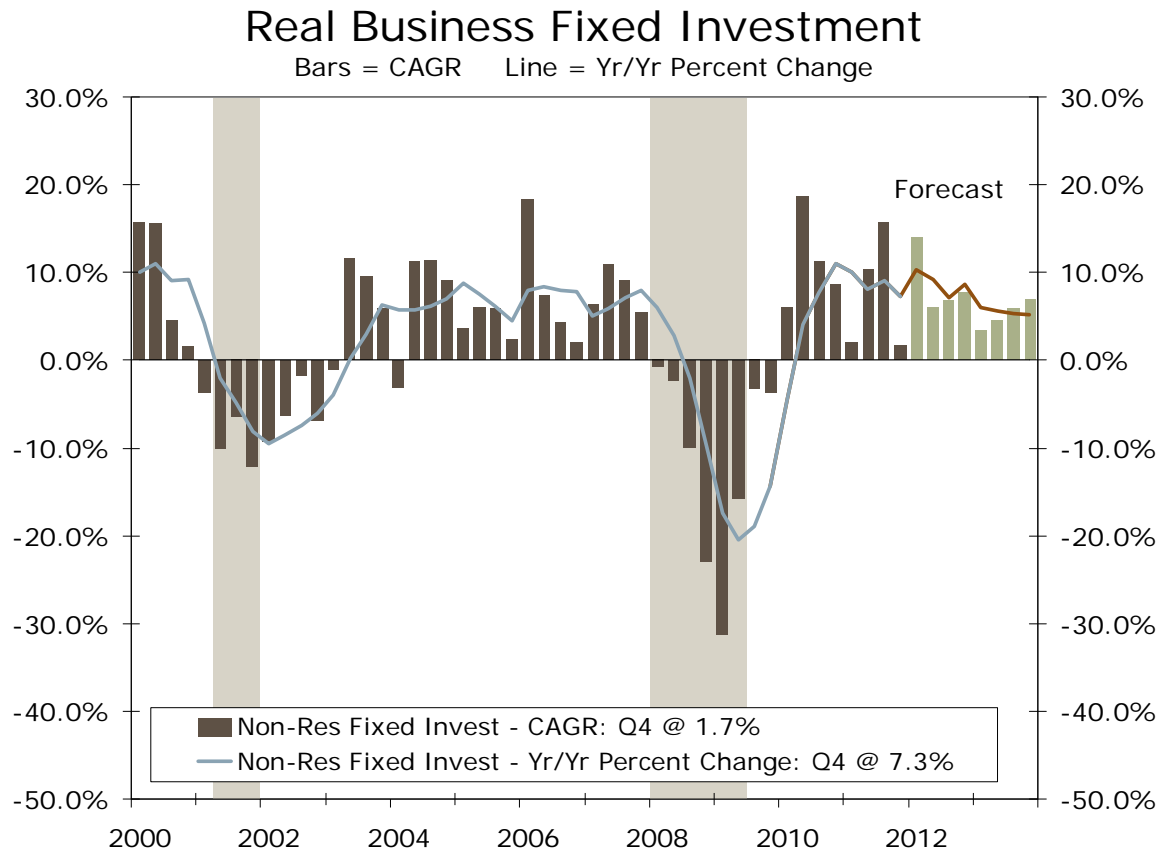
We are more than two years into the economic recovery and there is still a considerable amount of uncertainty regarding sovereign debt issues in Europe, the federal budget deficit and the U.S. housing sector



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

Capital Spending

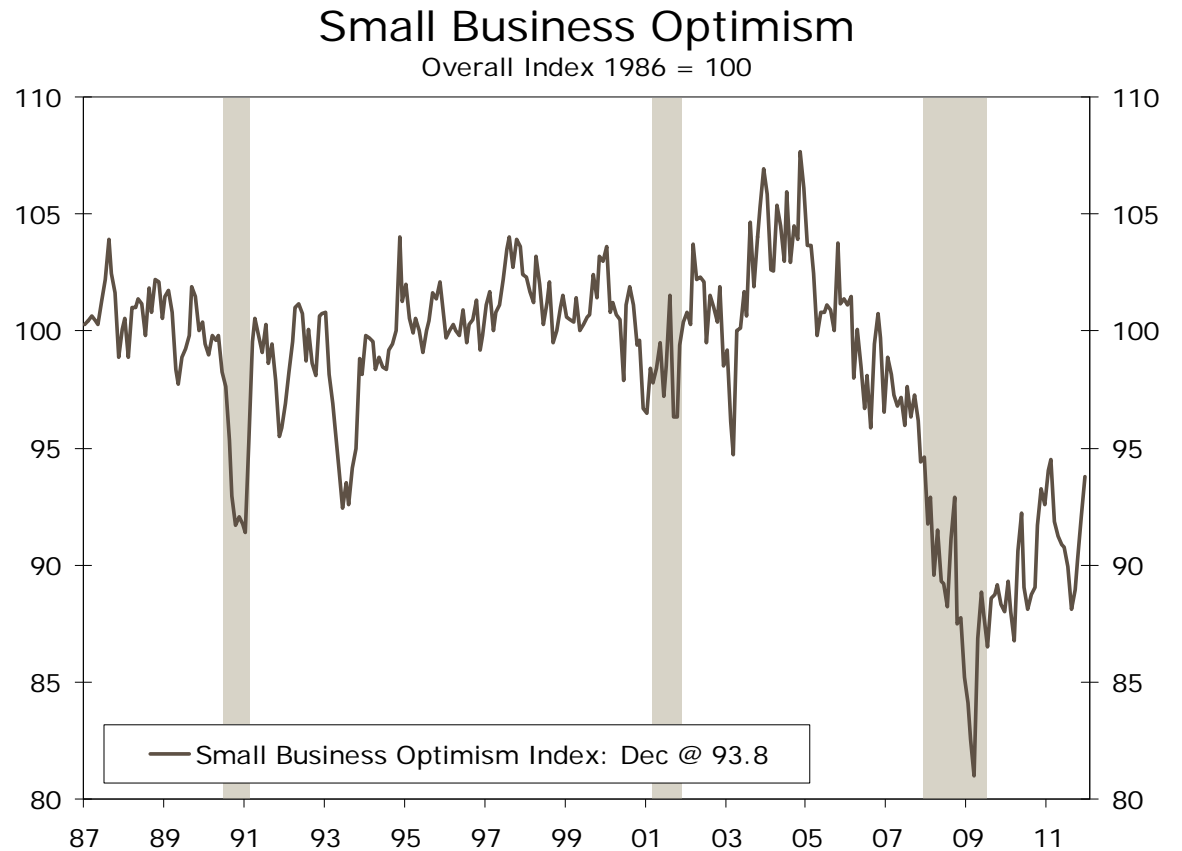
Business fixed investment spending will continue to add to overall growth



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

Small Businesses

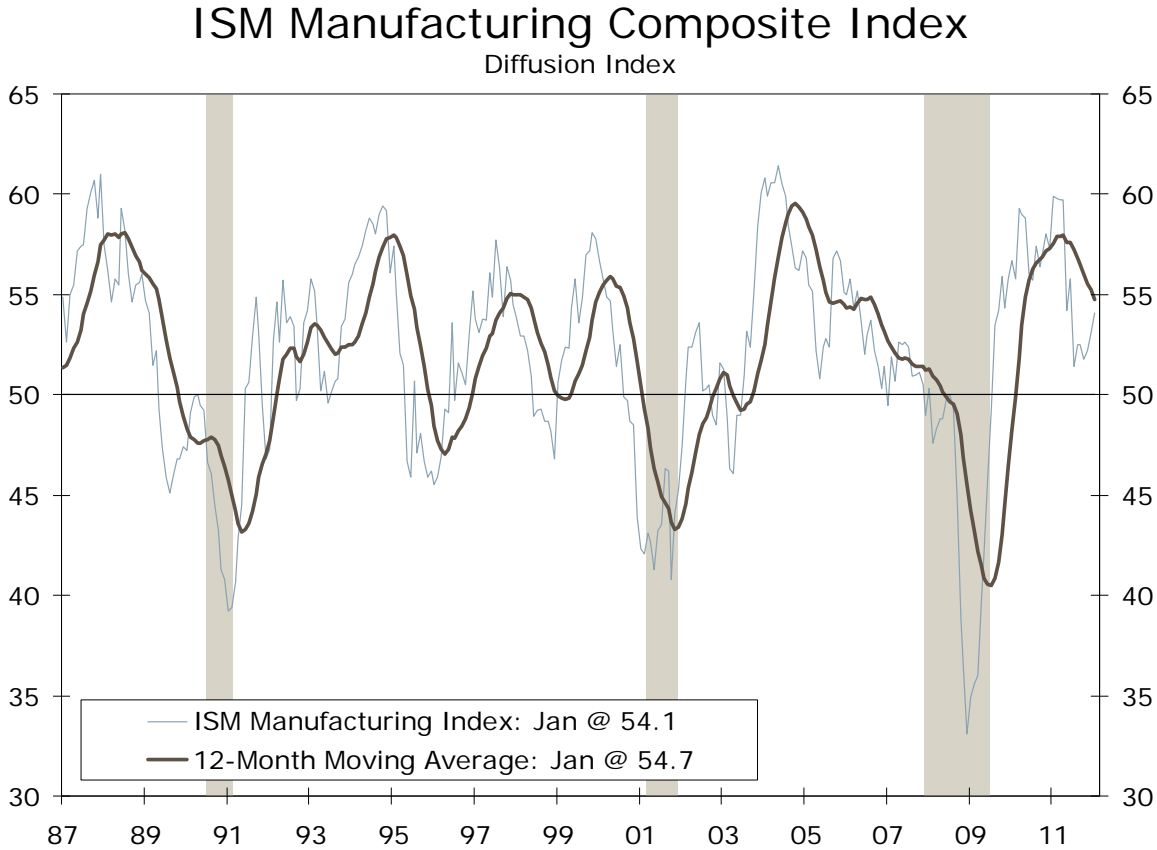
Small business confidence is slowly beginning to come back



Source: National Federation of Independent Businesses and Wells Fargo Securities, LLC

Manufacturing Sector

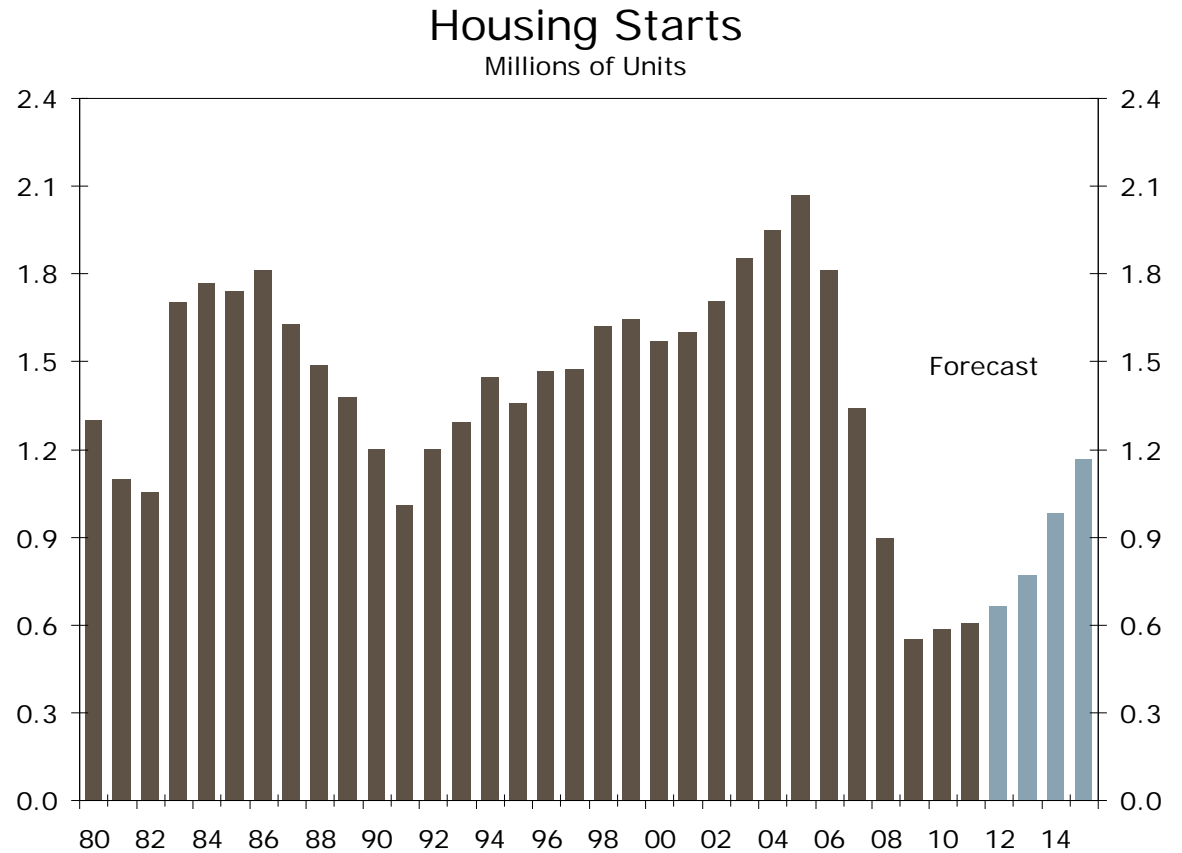
The manufacturing sector is seeing continued expansion in output, but the pace of expansion has slowed



Source: Institute for Supply Management and Wells Fargo Securities, LLC

Housing Market

Housing starts have bottomed and should begin to slowly pick up over the next few years



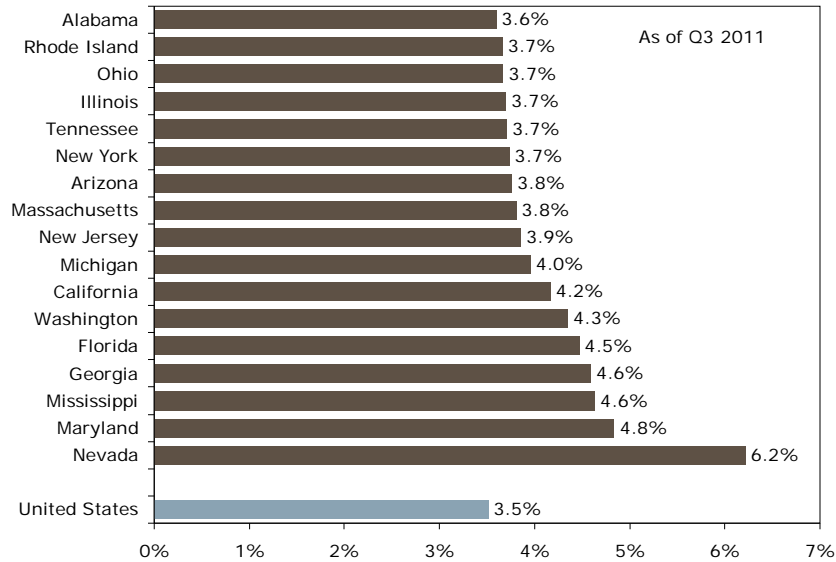
Source: U.S. Department of Commerce and Wells Fargo Securities, LLC

Delinquencies remain elevated. Inventories are working their way down after last decade's enormous buildup.

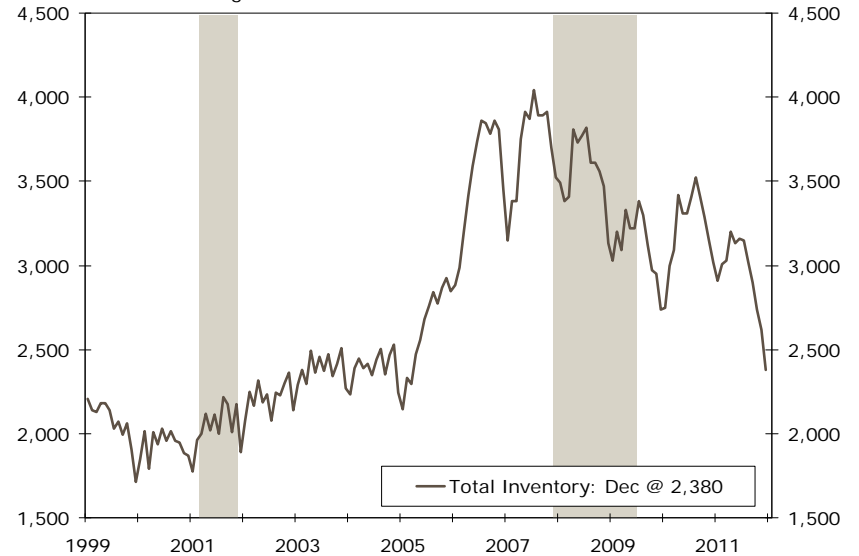
Delinquencies

Inventory

Mortgages 90+ Days Delinquent - By State
Percent of Mortgages Outstanding



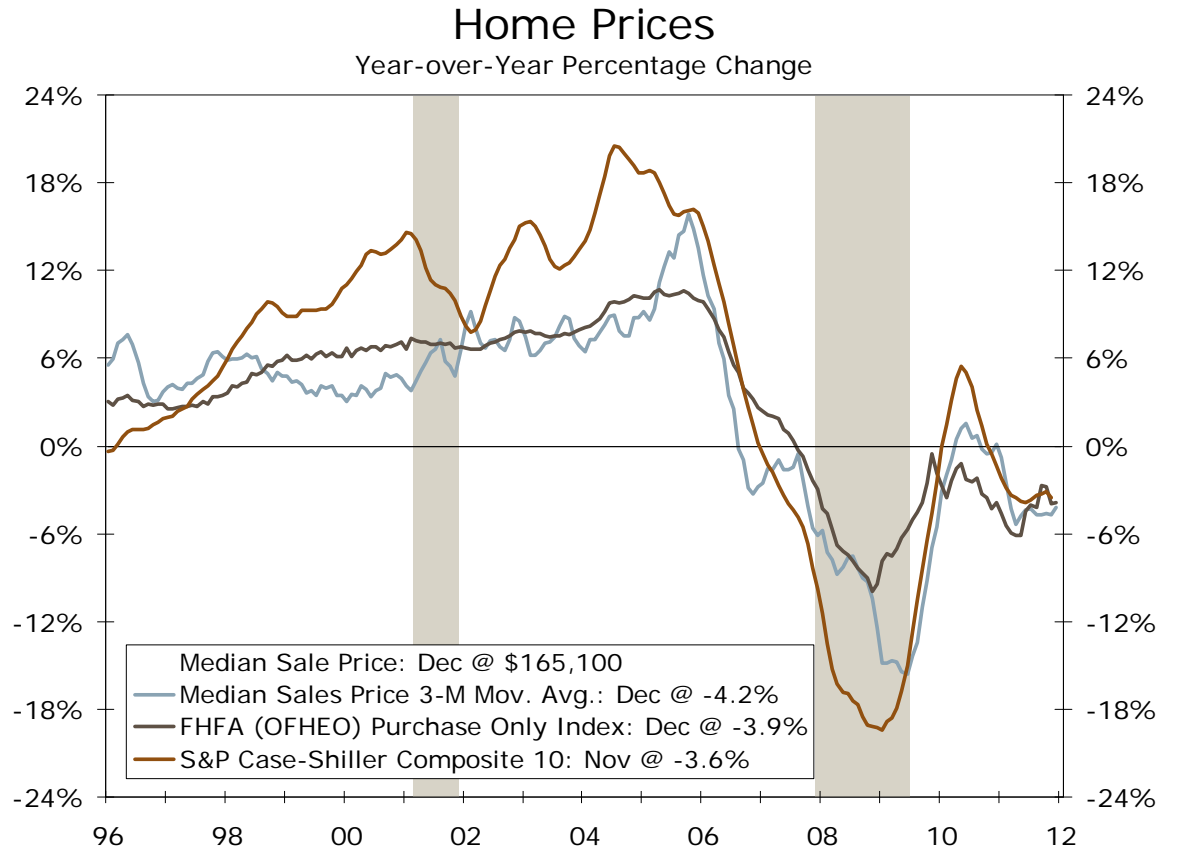
Inventory of Existing Homes for Sale
Existing Homes for Sale at End of Month - In Thousands



Source: Mortgage Bankers Association, National Association of Realtors and Wells Fargo Securities, LLC

Housing Market

Various mortgage foreclosure moratoriums and stimulus programs likely supported prices earlier, but are now giving way

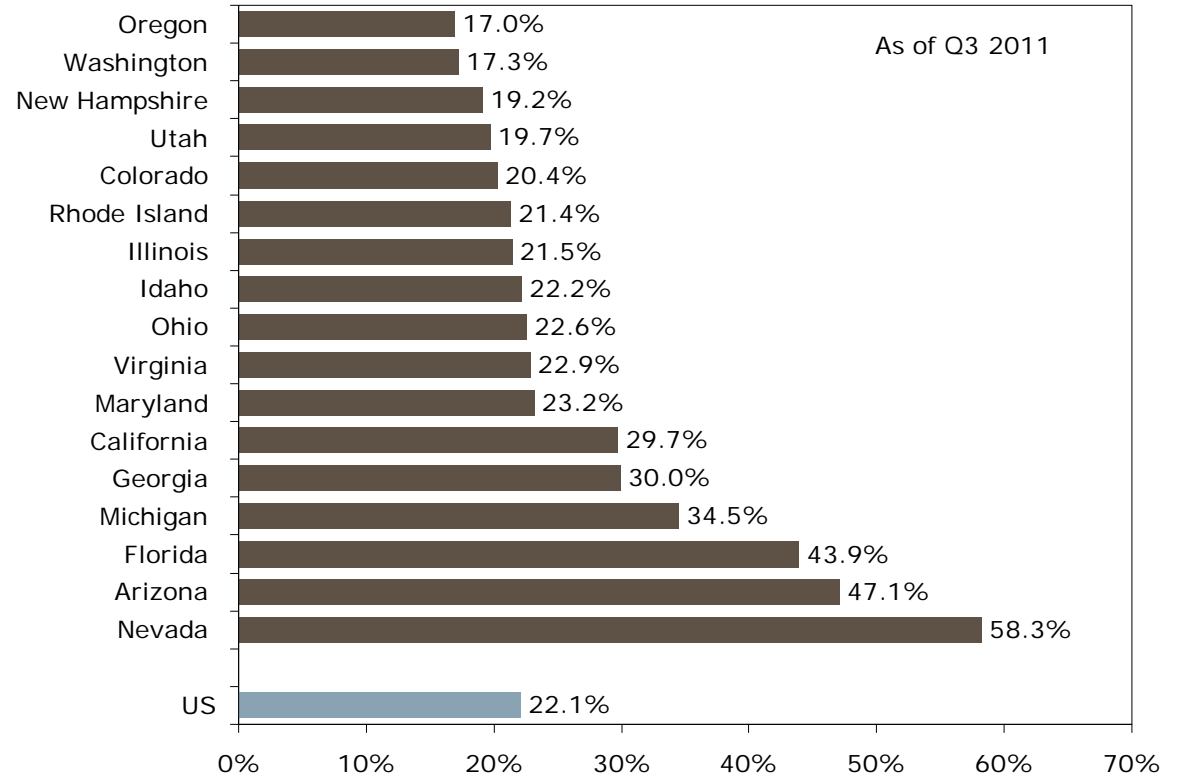


Source: Federal Housing Finance Agency, National Association of Realtors, S&P Corp. and Wells Fargo Securities, LLC

Negative equity in homes has contributed to foreclosures and reduced labor mobility

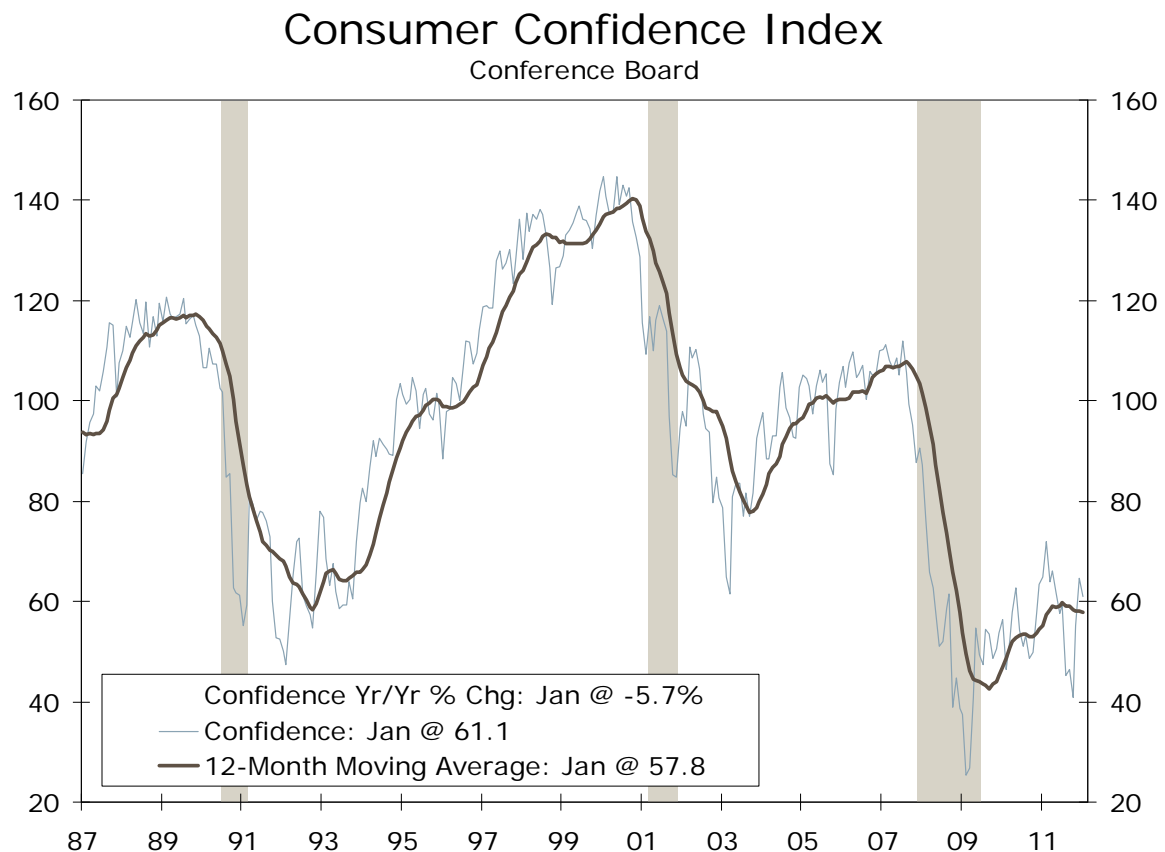
Negative Equity Mortgages - By State

Percent of Mortgages Outstanding



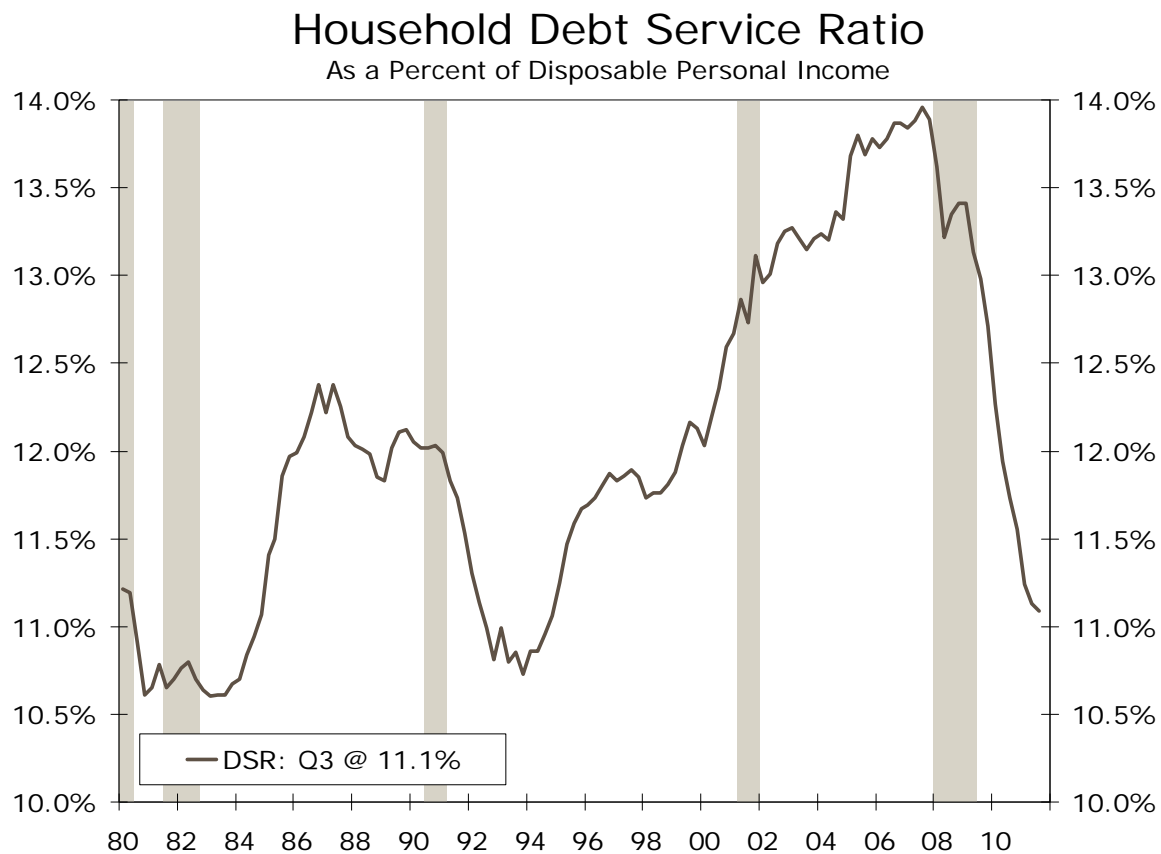
Source: CoreLogic and Wells Fargo Securities, LLC

Consumers are still struggling to find reasons to be confident



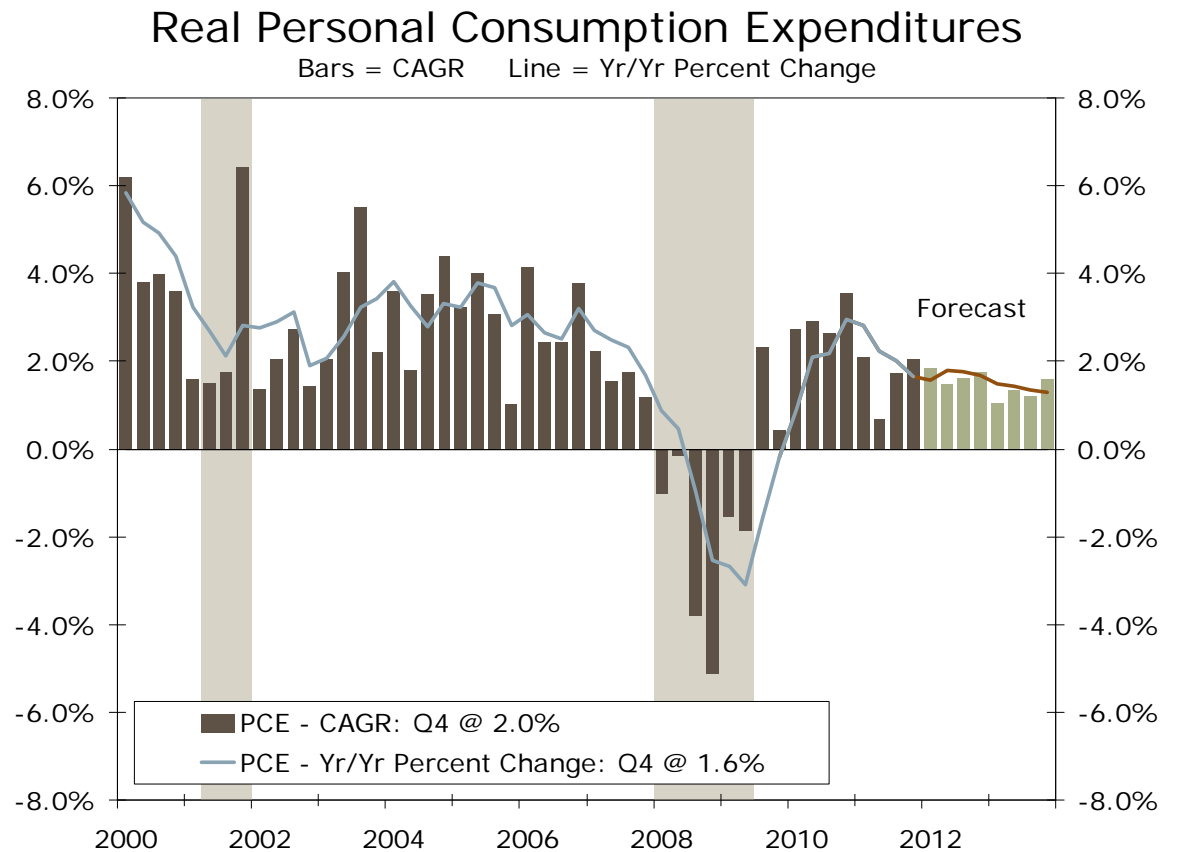
Source: The Conference Board and Wells Fargo Securities, LLC

Debt service has returned to more sustainable rates



Source: Federal Reserve Board and Wells Fargo Securities, LLC

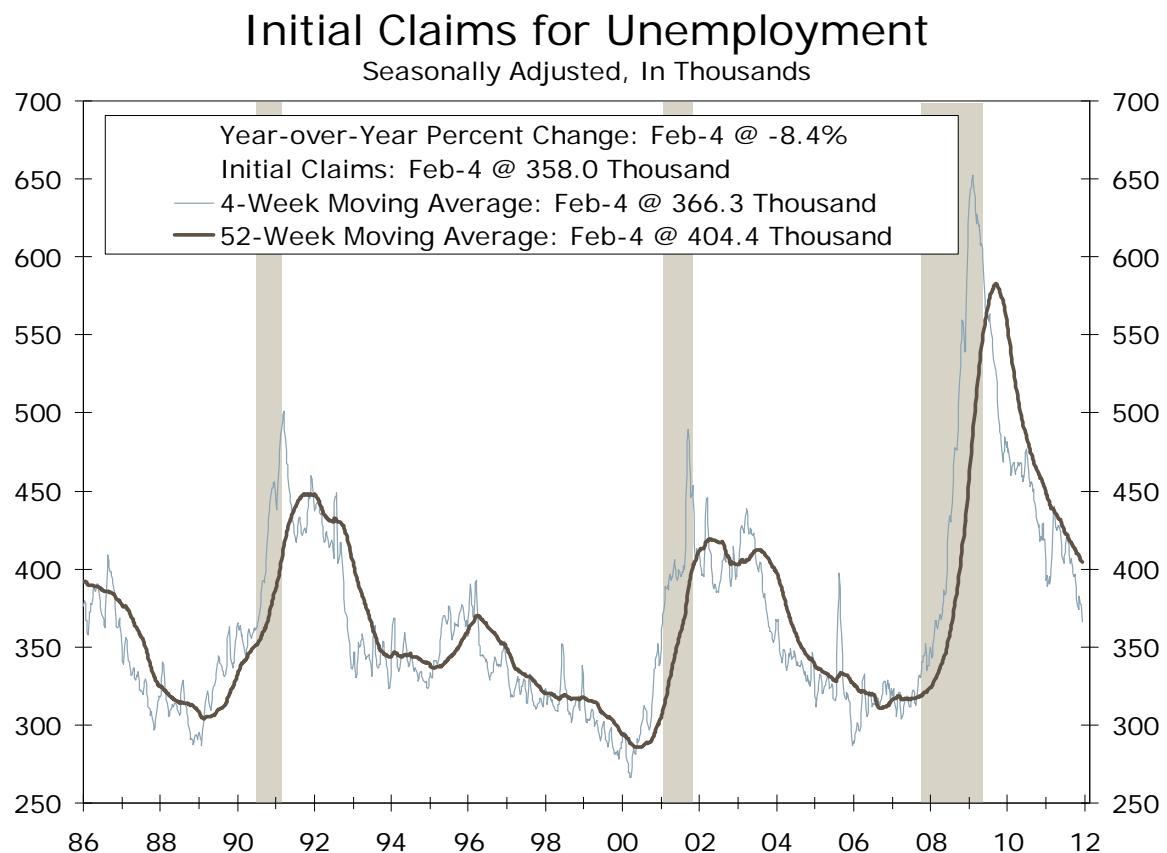
Consumer spending will remain subdued until the end of 2013



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

The Employment Situation

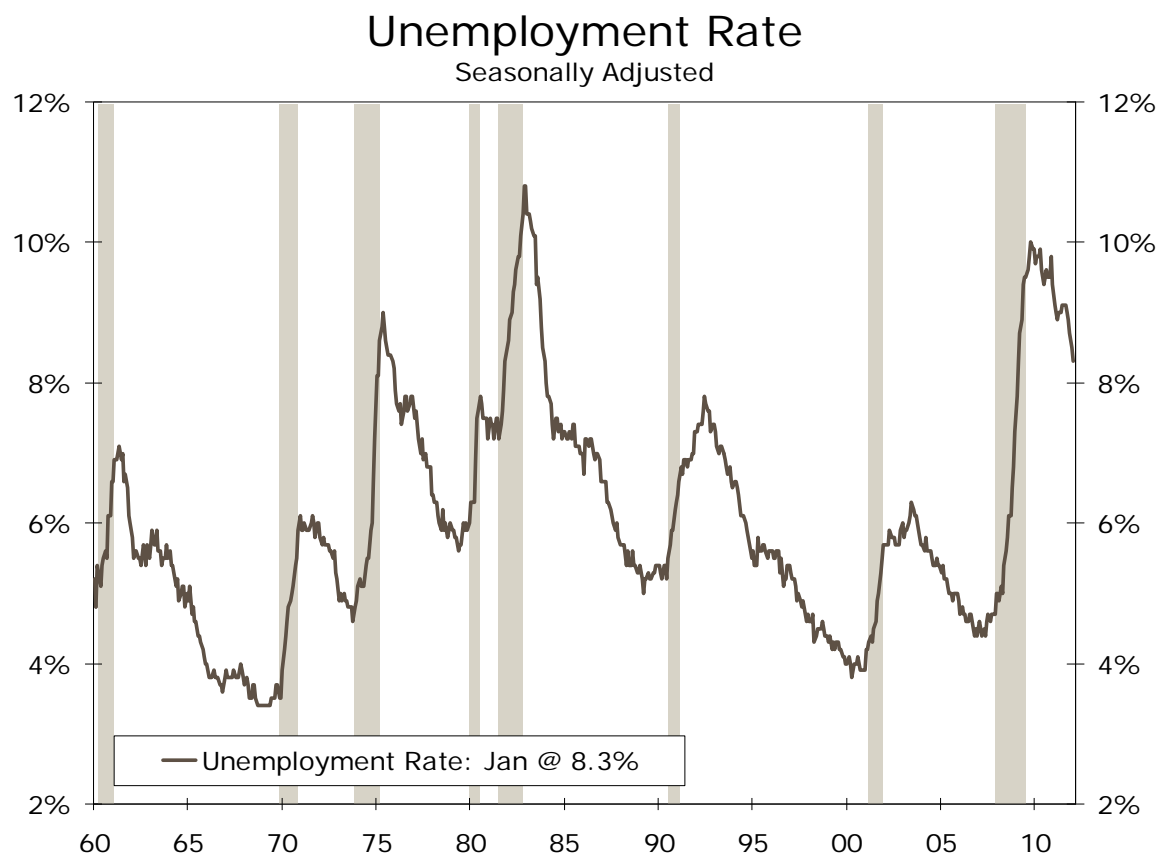
Initial claims data have been signaling an improvement



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

The Employment Situation

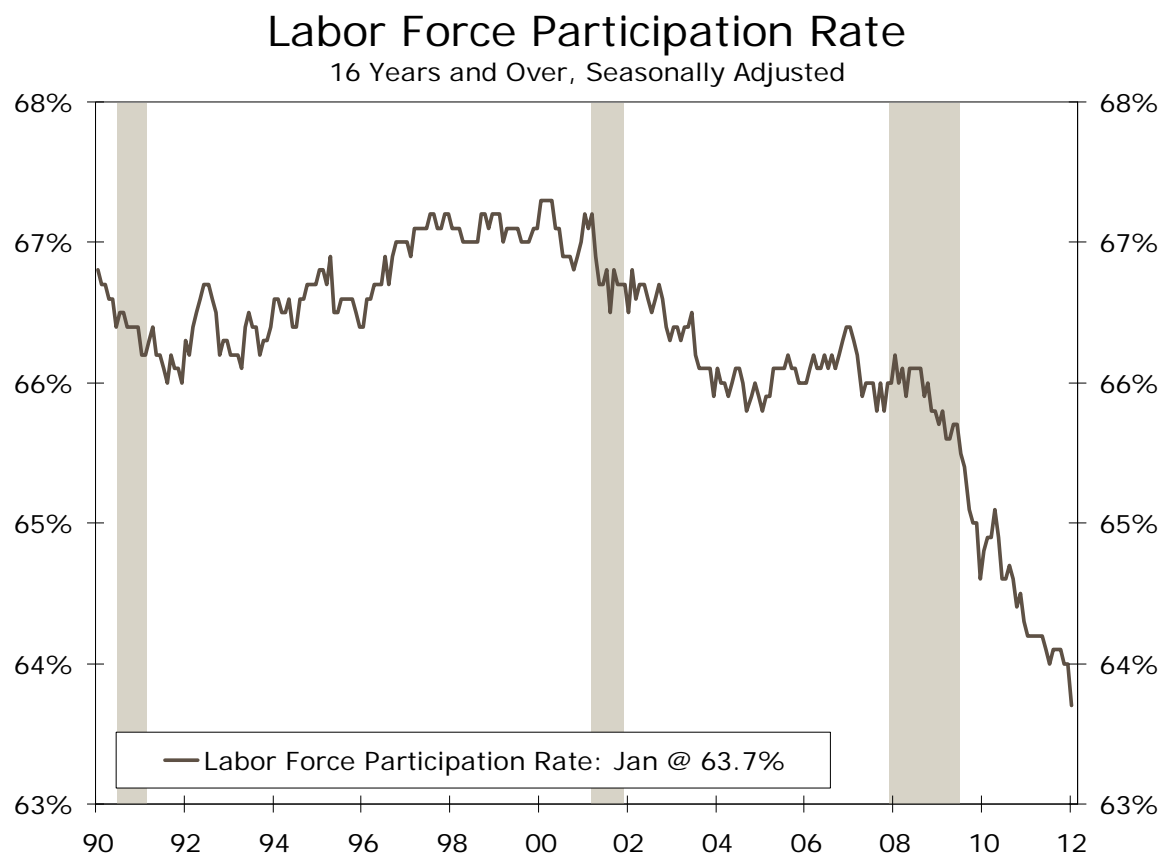
The unemployment rate is falling, but mostly for the wrong reasons



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

The Employment Situation

The reason for the decline in the unemployment rate is tied to the drop-off in labor force participation



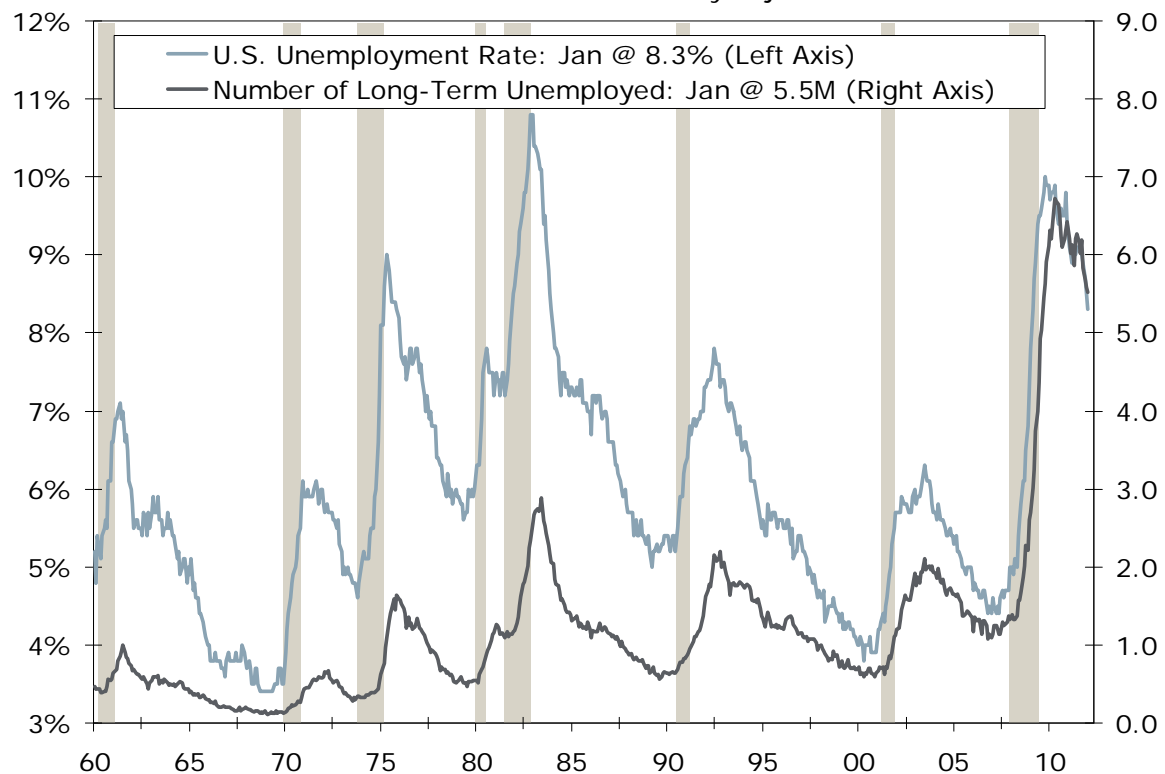
Source: U.S. Department of Labor and Wells Fargo Securities, LLC

The Employment Situation

Not only is unemployment remaining exceptionally high, but a large number of people have remained unemployed for a long period of time

Unemployment and Long-Term Unemployment

Percent, In Millions, Seasonally Adjusted



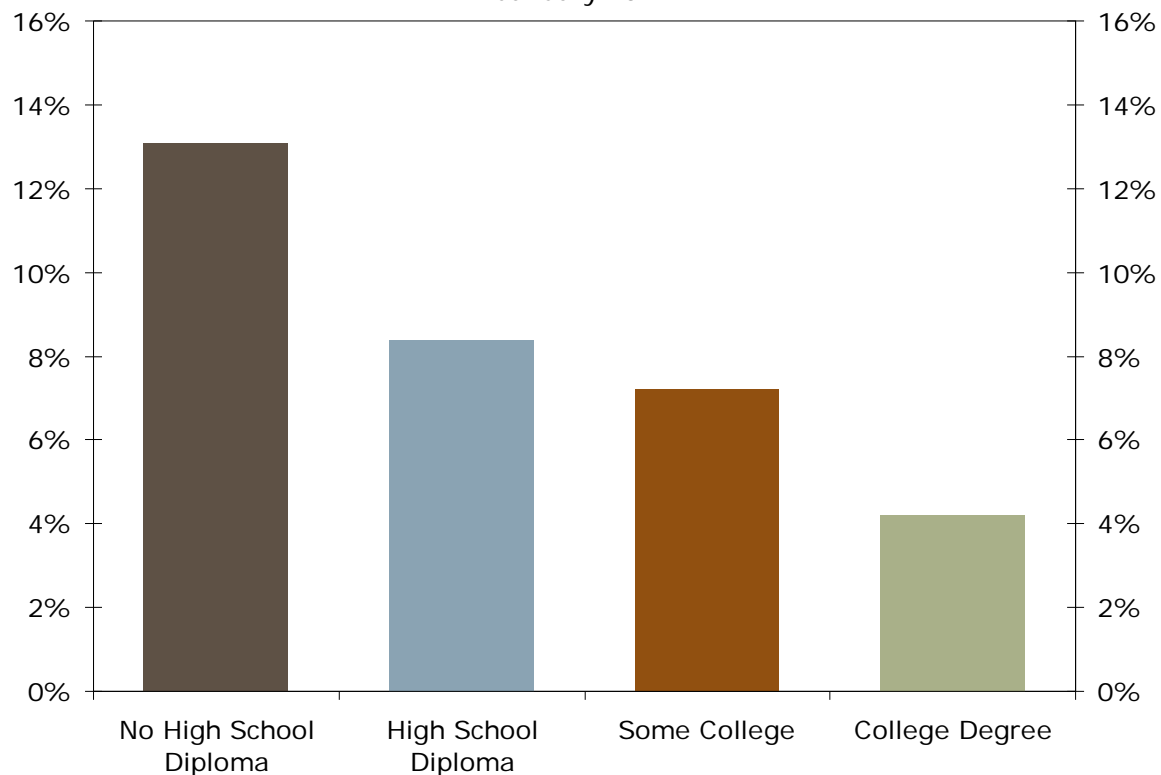
Source: U.S. Department of Labor and Wells Fargo Securities, LLC

The Employment Situation

The unemployment rate for college-educated workers remains low at 4.2 percent, while the unemployment rate for workers with less than a high school diploma is 13.1 percent

Unemployment Rate by Education Level

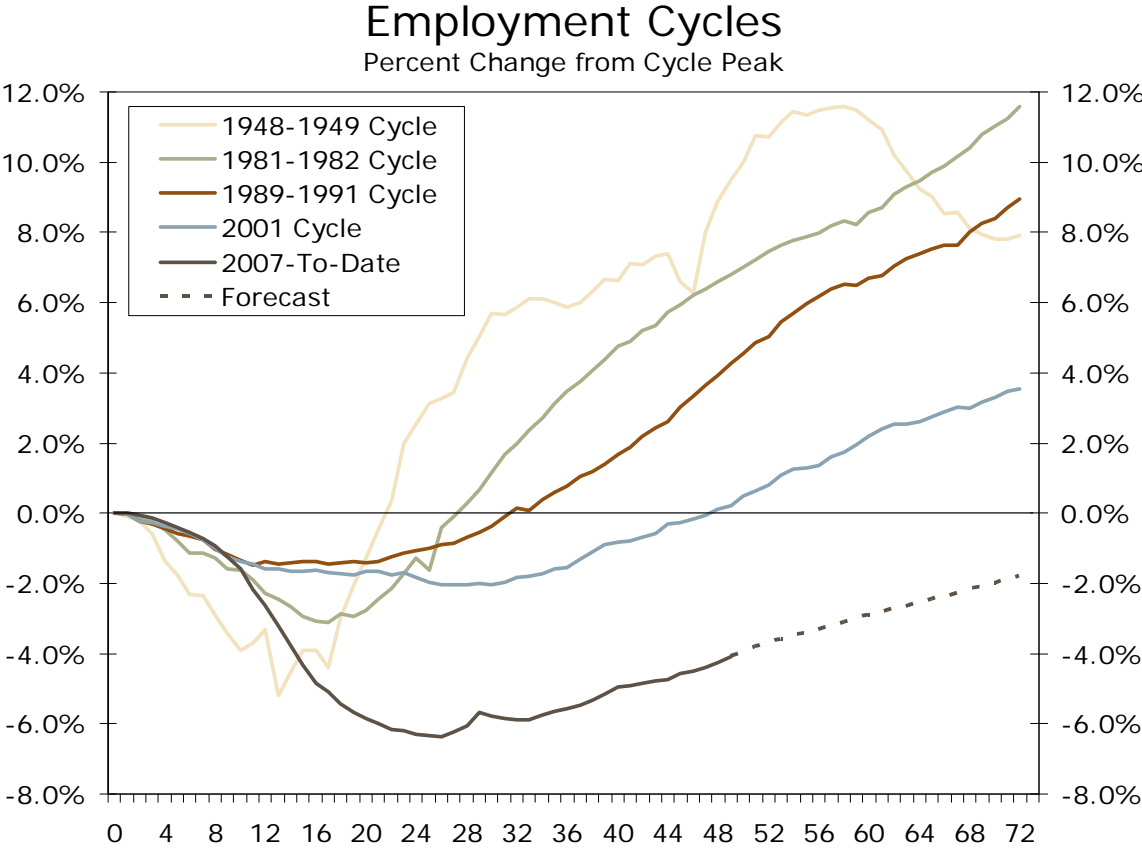
January 2012



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

The Employment Situation

Employment will eventually
regain its peak, but not quickly

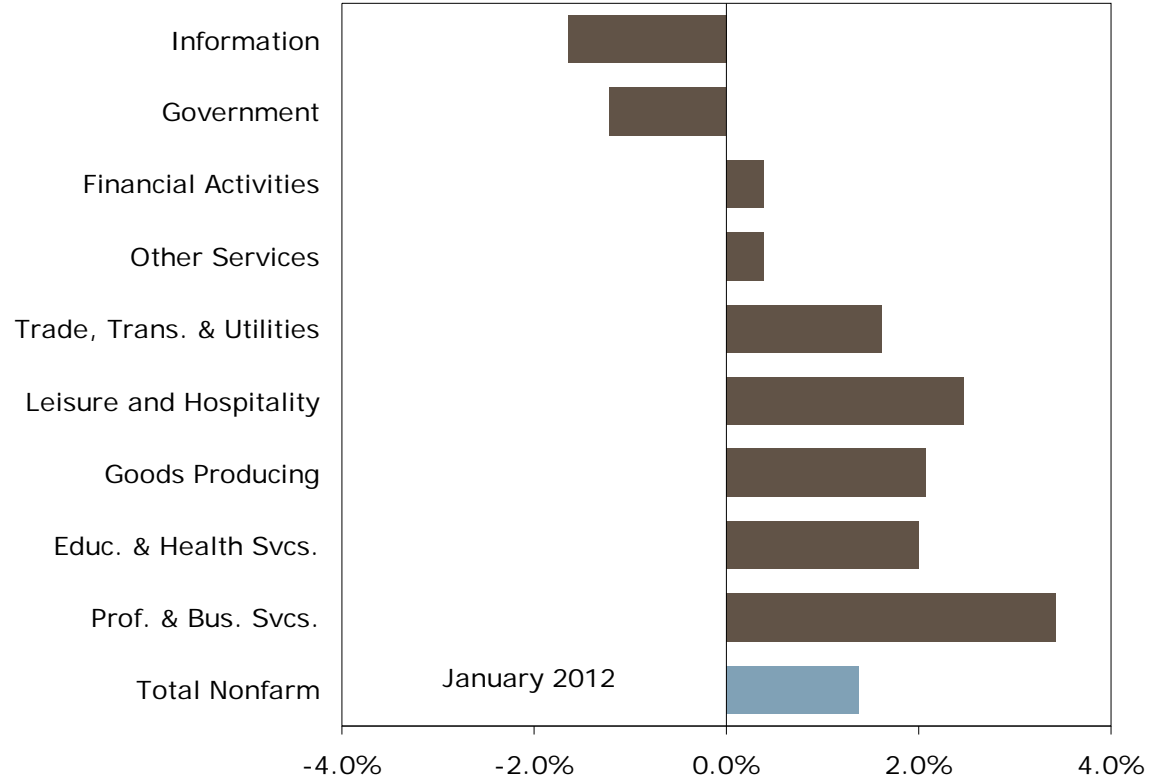


Source: U.S. Department of Labor and Wells Fargo Securities, LLC

Where is the Job Growth?

The service sector continues to lead job growth

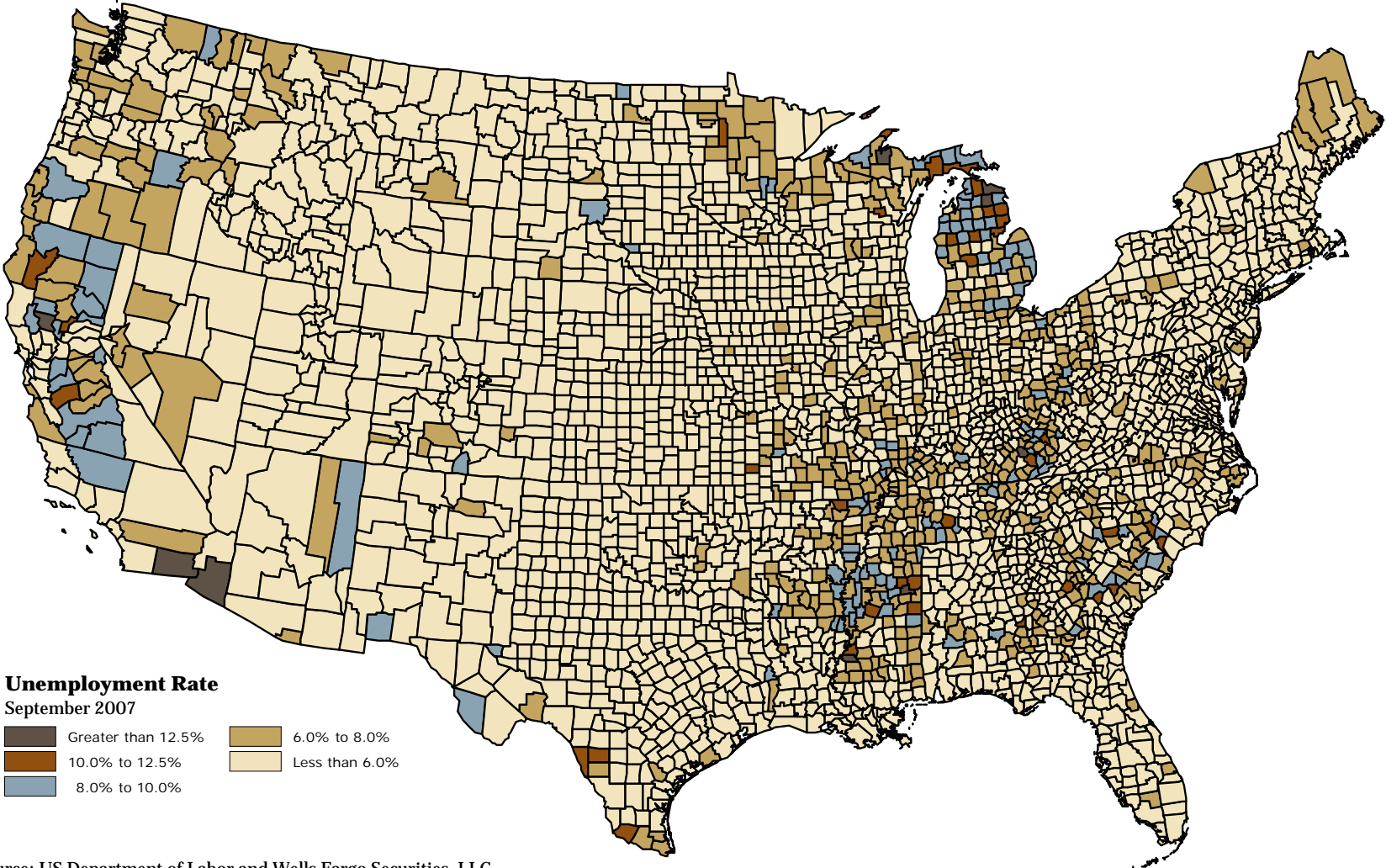
United States Employment by Industry
Year-over-Year Percent Change, 3-Month Moving Average



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

Unemployment by County

Unemployment Rate

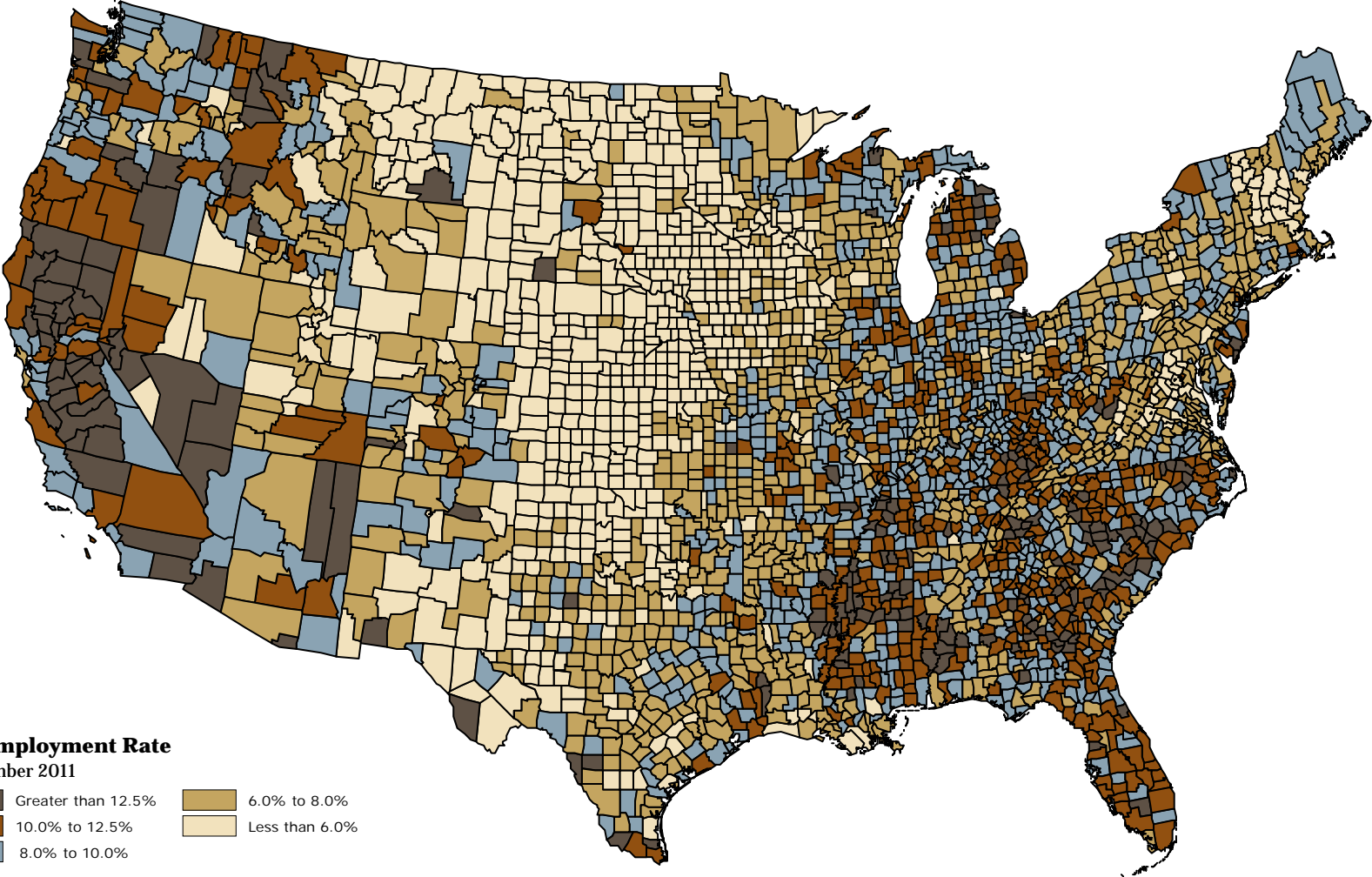


Source: US Department of Labor and Wells Fargo Securities, LLC

Unemployment by County

Large Portions of the United States Continue to Face Serious Unemployment Issues

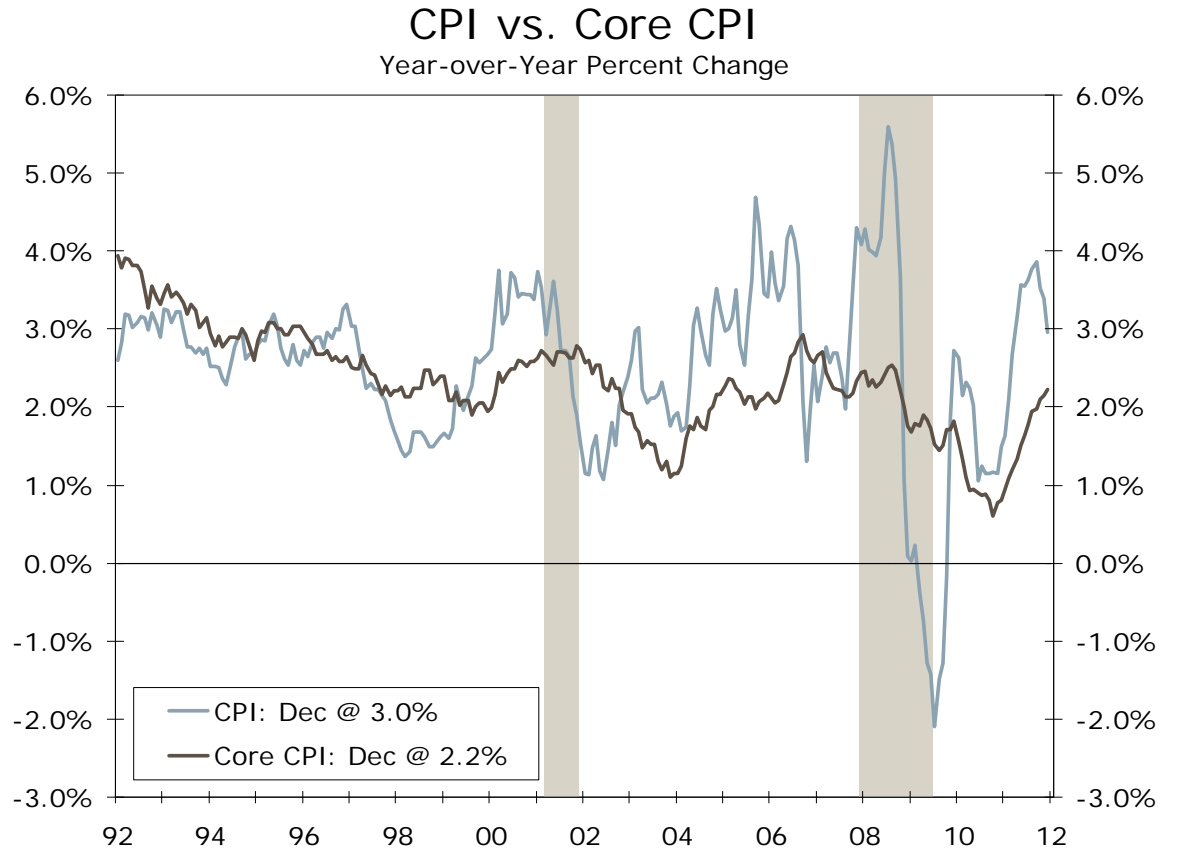
Unemployment Rate



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

Inflation

Inflation is beginning to show signs of leveling off



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

Interest Rate Outlook

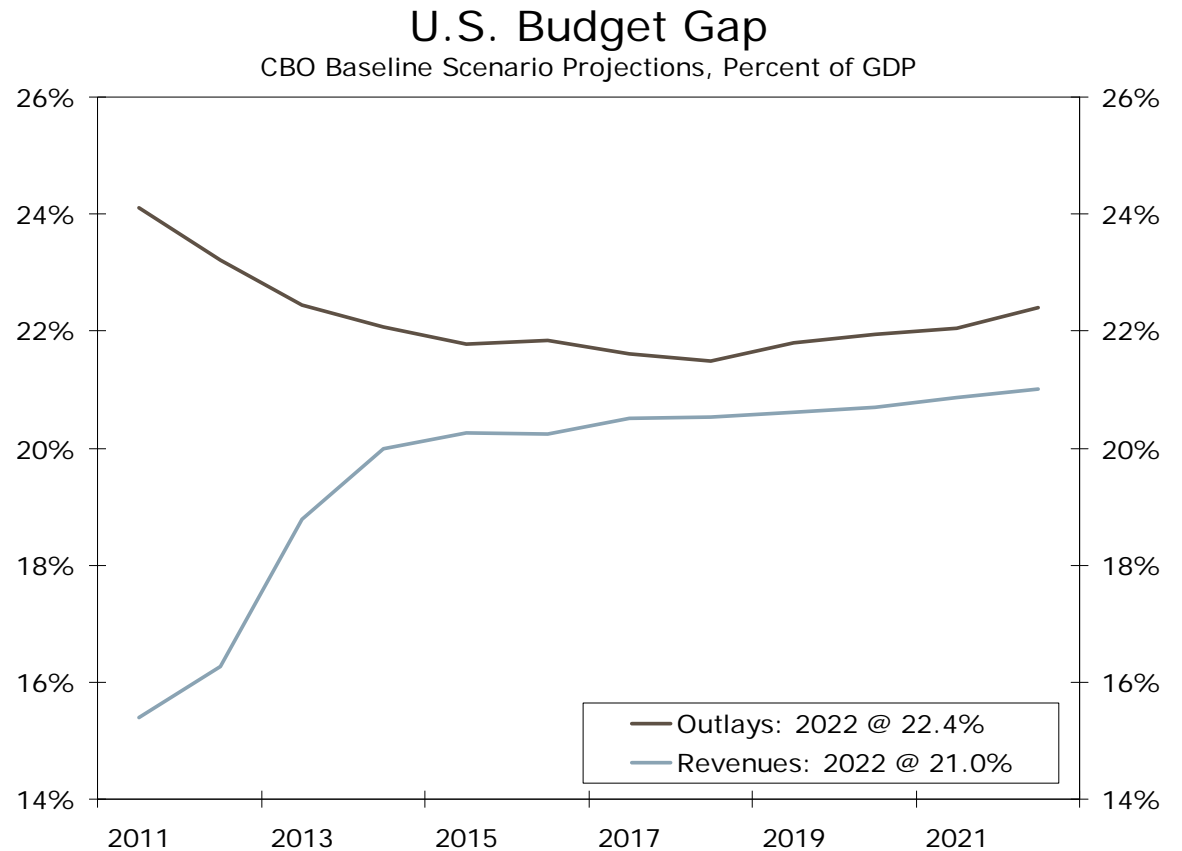
Rates will move higher, but will do so very slowly



Source: Federal Reserve Board and Wells Fargo Securities, LLC

What is Going on in D.C.?

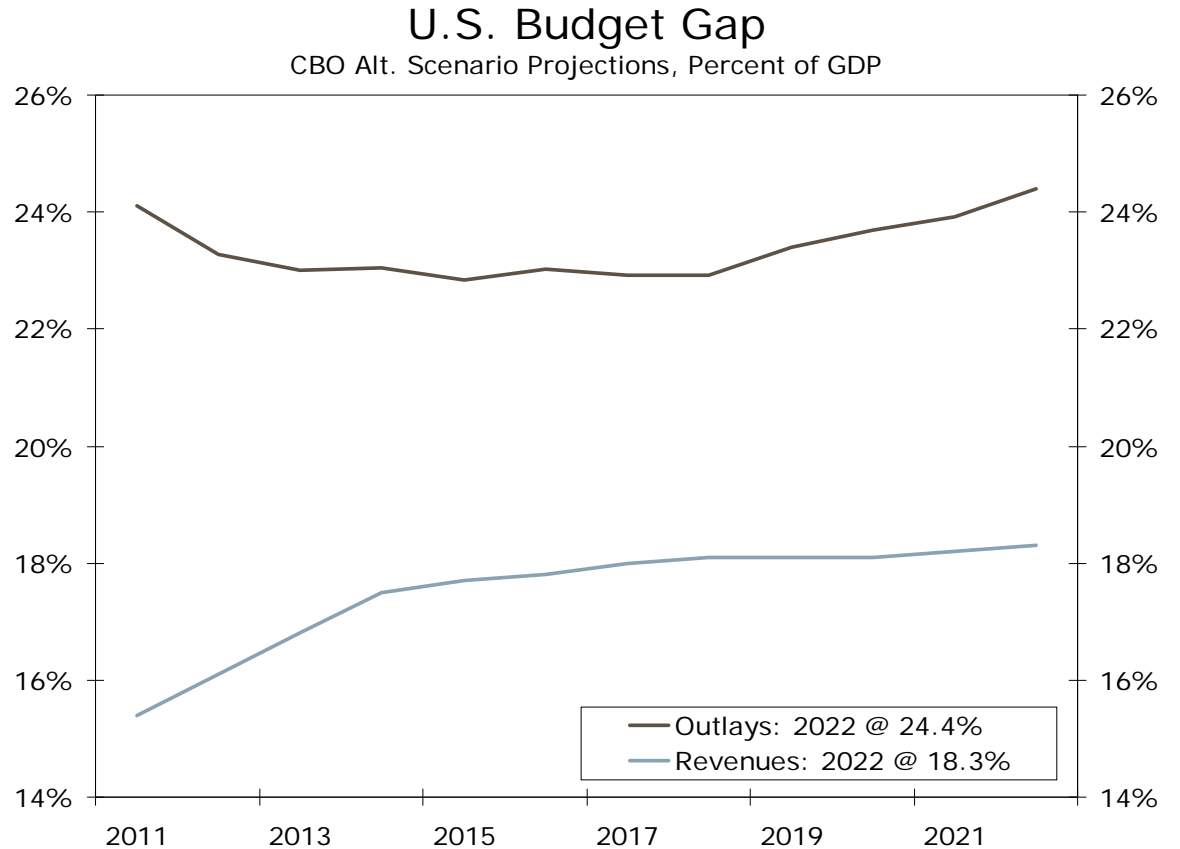
Even under existing law, with budget cuts and tax increases, there is still a budget gap



Source: Congressional Budget Office and Wells Fargo Securities, LLC

What is Going on in D.C.?

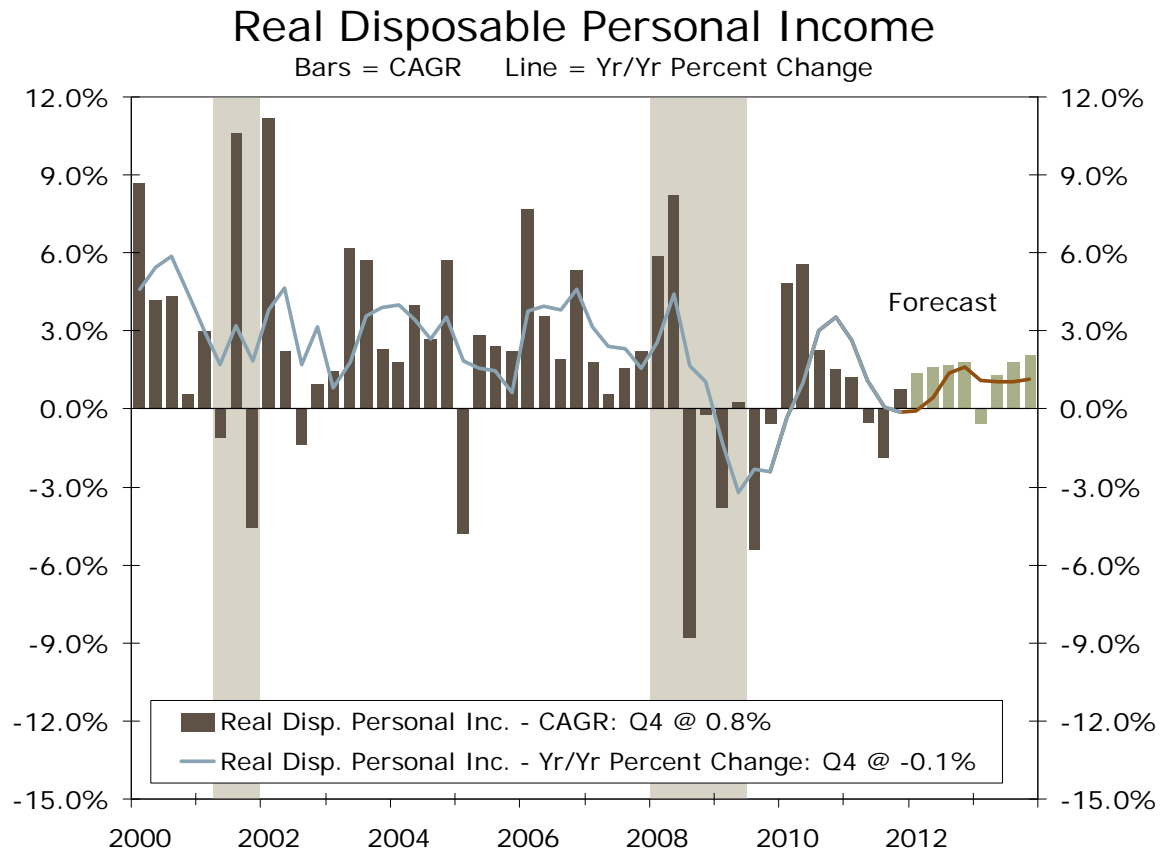
If spending cuts are not enacted and tax increases do not occur, the budget gap swells



Source: Congressional Budget Office and Wells Fargo Securities, LLC

Fiscal Policy Changes in 2013

Under existing law, significant fiscal policy changes in 2013 would put downward pressure on disposable income

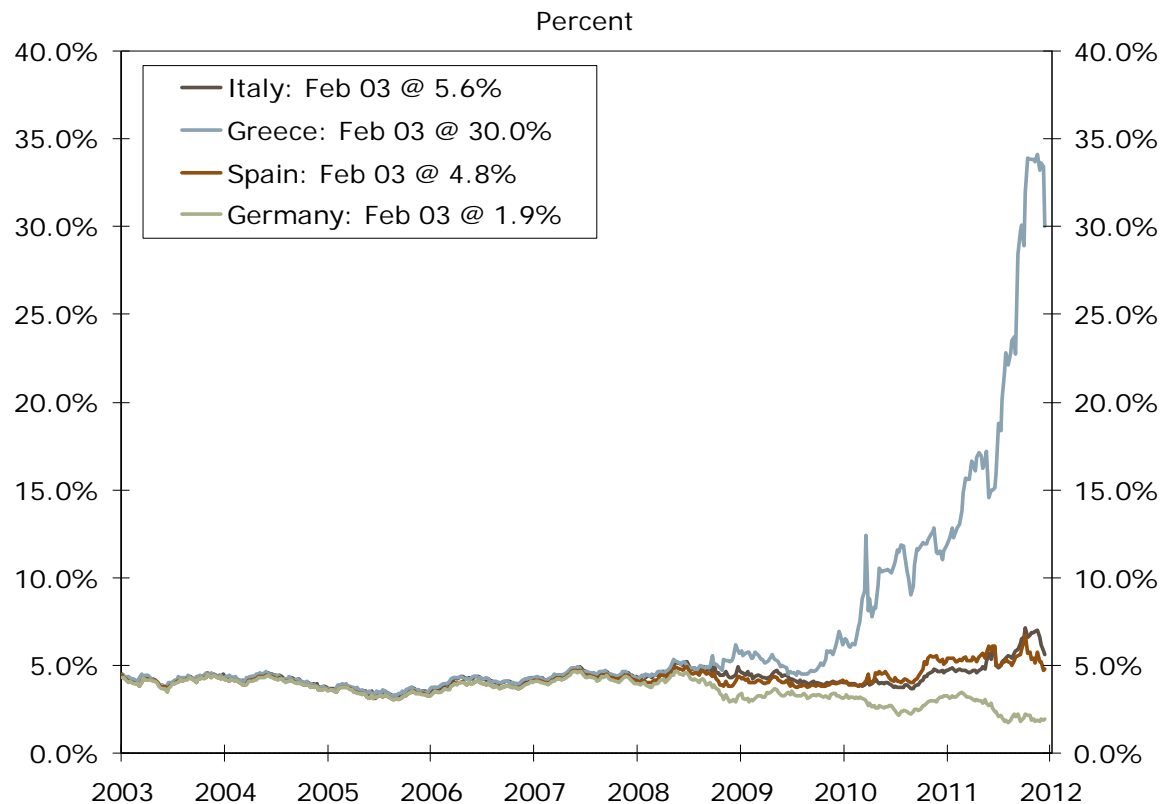


Source: U.S. Department of Commerce and Wells Fargo Securities, LLC

The European Sovereign Debt Crisis

The European debt crisis remains the greatest risk to our economic outlook. Borrowing rates remain elevated across the Eurozone. Italy is the most worrisome country, with nearly €2 trillion in debt outstanding.

10-Year Government Bond Yields



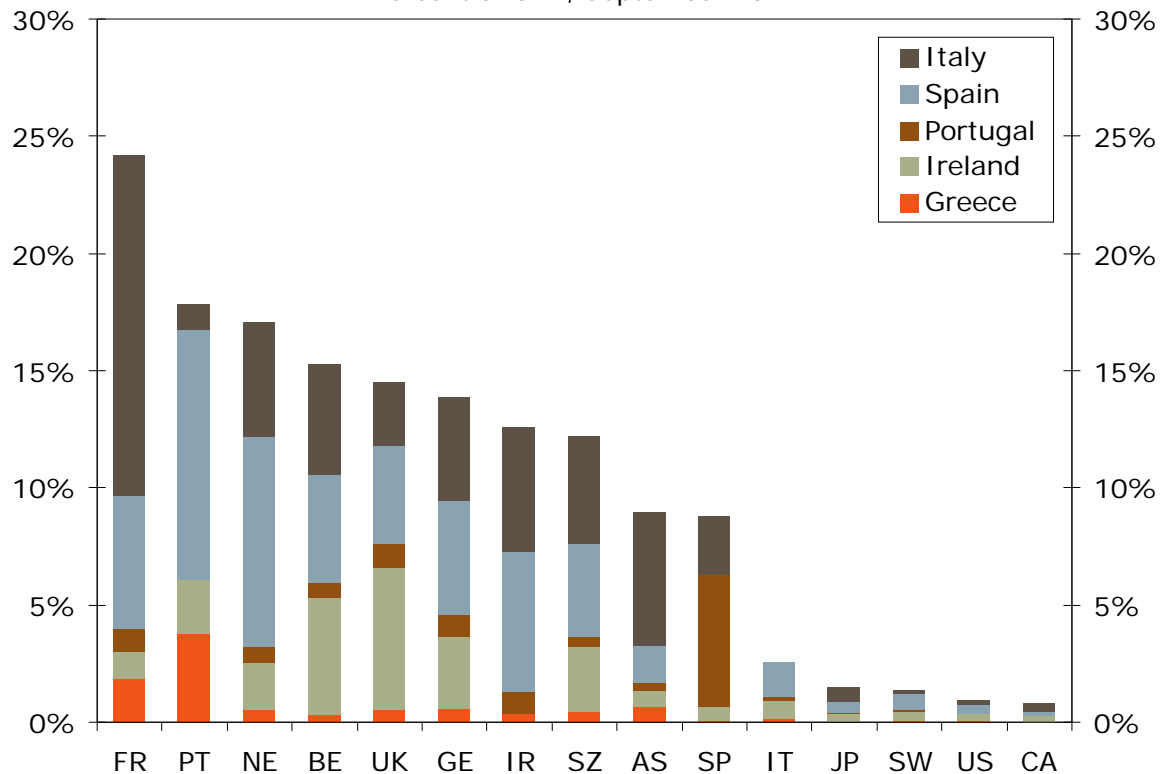
Source: IHS Global Insight and Wells Fargo Securities, LLC

The European Sovereign Debt Crisis: Peripheral Exposure

Many European countries have significant exposure to sovereign debt in peripheral European countries

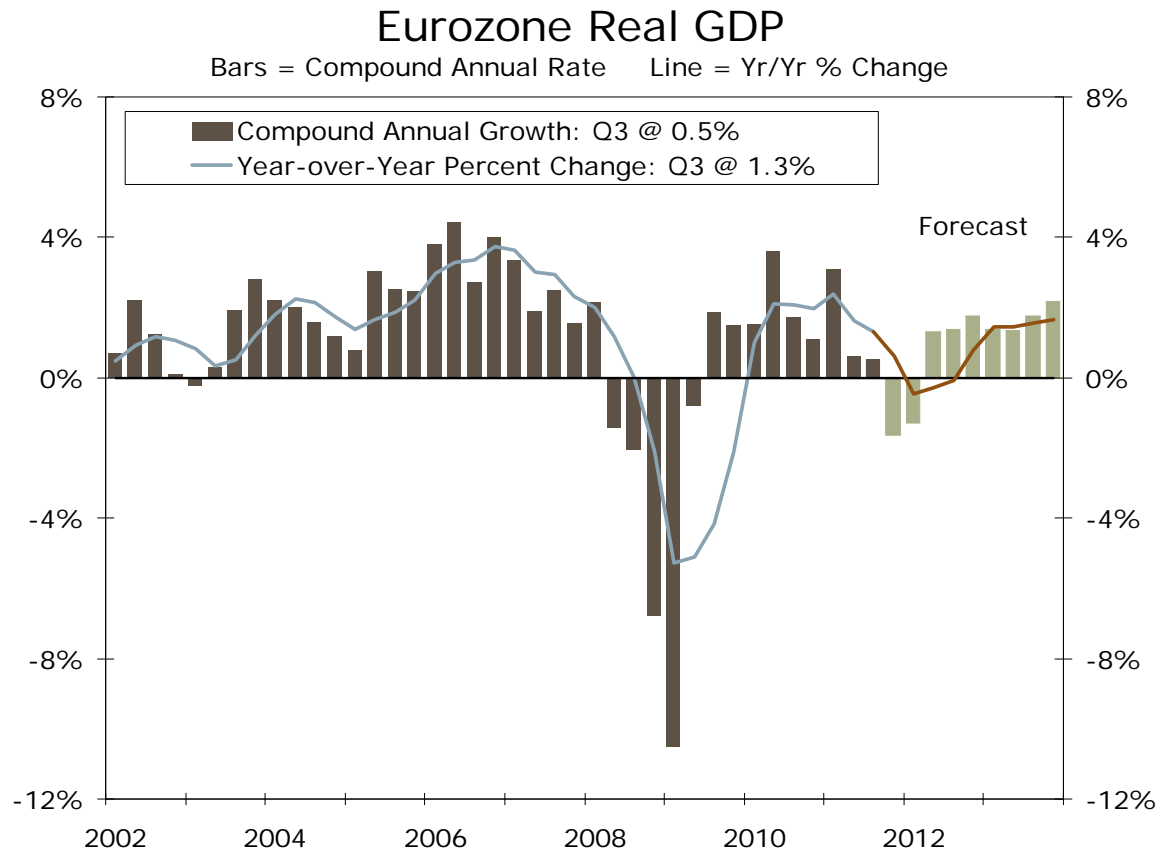
Bank Exposure to Peripheral Europe

Percent of GDP, September 2011



Source: Bank for International Settlements and Wells Fargo Securities, LLC

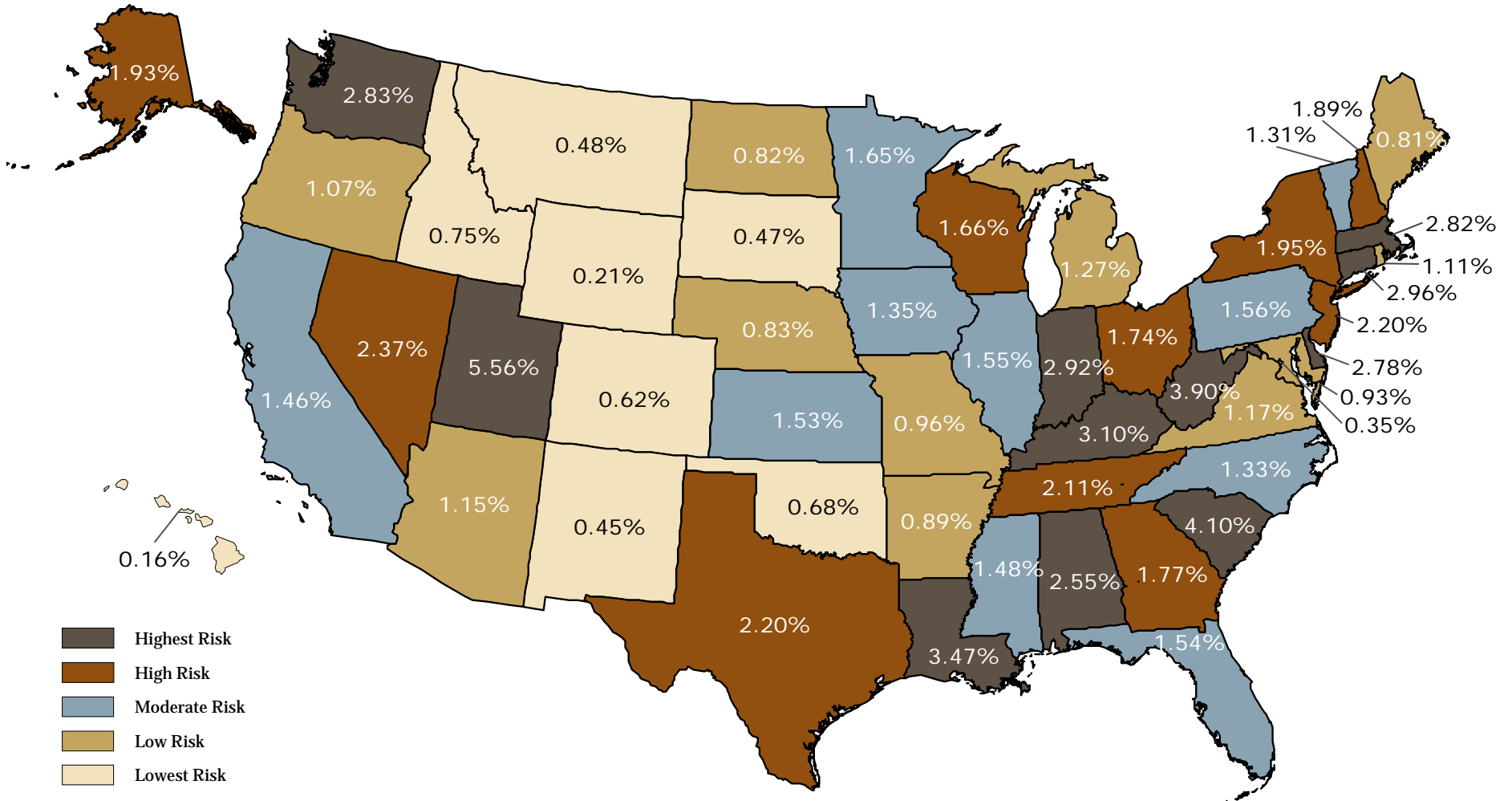
The overall euro area appears to be slipping back into recession



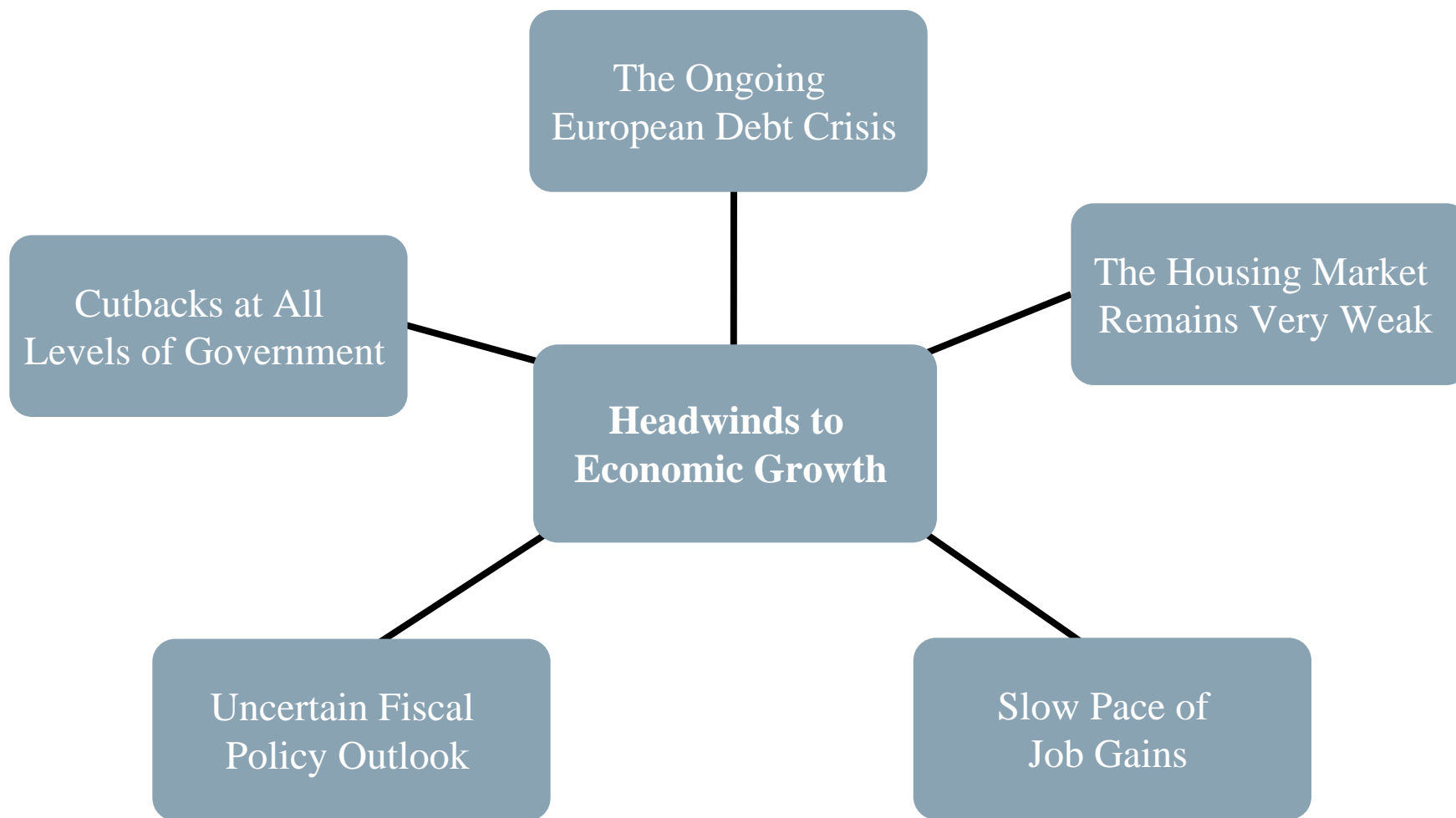
Source: IHS Global Insight and Wells Fargo Securities, LLC

Impact of A European Recession on the U.S.

European Exports as a Percent of GDP



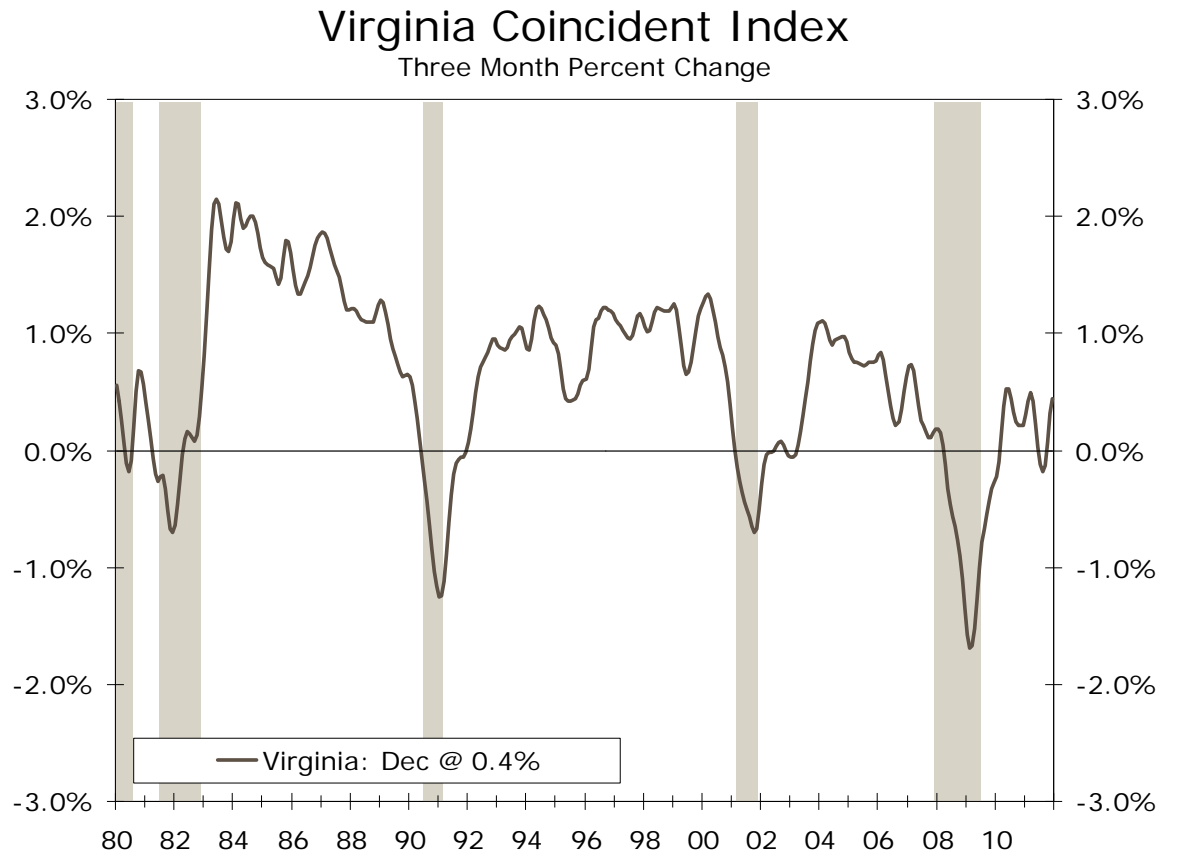
Headwinds to Economic Growth



The Virginia Economy

Virginia – Current Economic Conditions

Growth across the state is slow, but remains positive



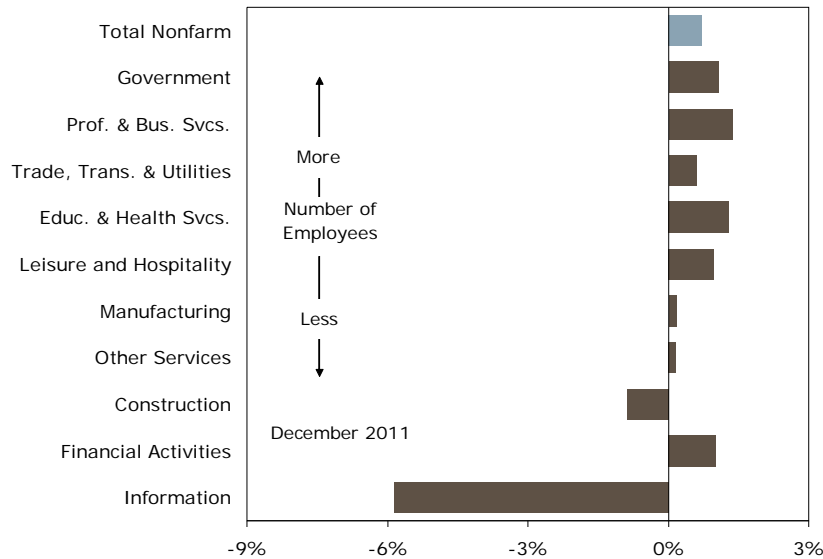
Source: Federal Reserve Bank of Philadelphia and Wells Fargo Securities, LLC

Virginia – Employment Growth & Unemployment Rate

Job growth is slowly picking up, led by the business and professional services sector. The unemployment rate remains far below the national average.

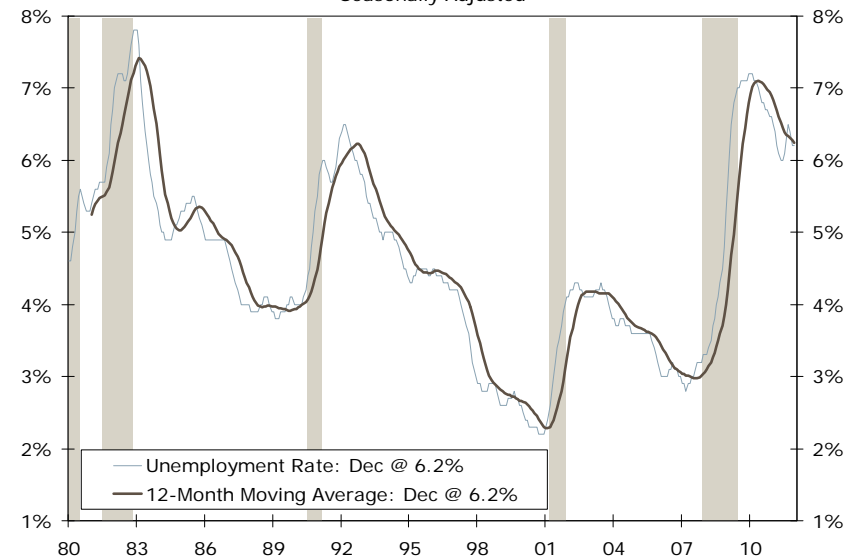
Employment

Virginia Employment Growth by Industry
Year-over-Year Percent Change of 3-M Moving Average



Unemployment Rate

Virginia Unemployment Rate
Seasonally Adjusted

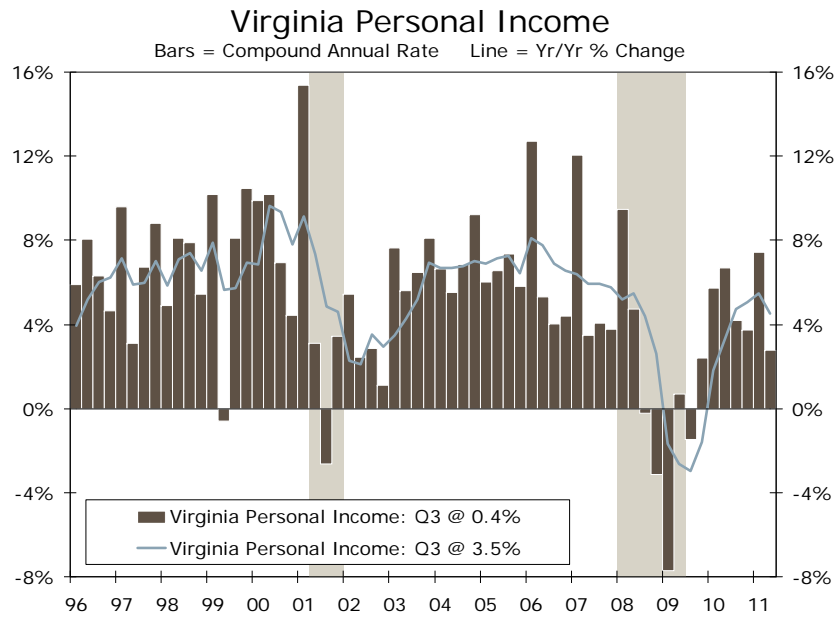


Source: U.S. Department of Labor and Wells Fargo Securities, LLC

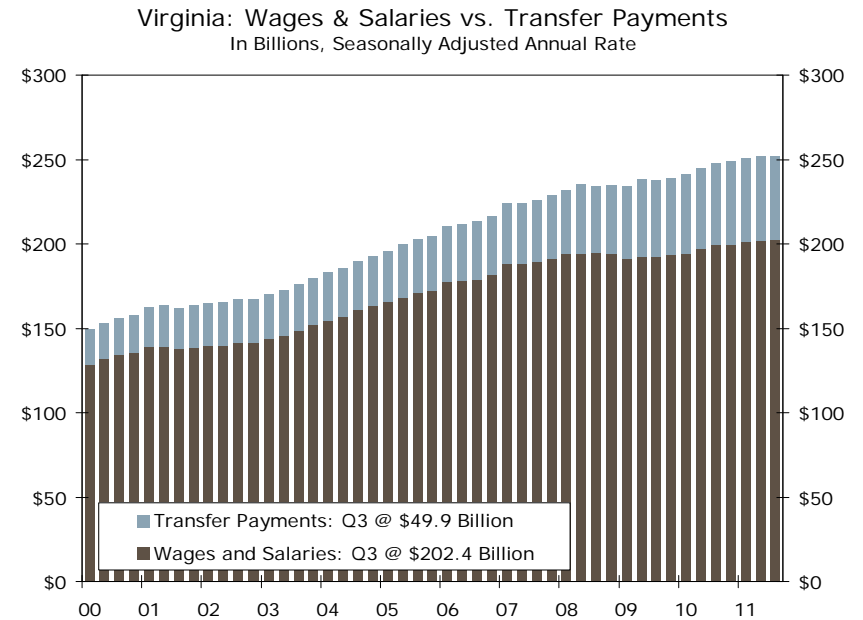
Virginia – Personal Income Situation

Personal income growth in Virginia has rebounded nicely. Unfortunately, wage and salary growth within the state has been flat.

Personal Income



Composition of Income Growth

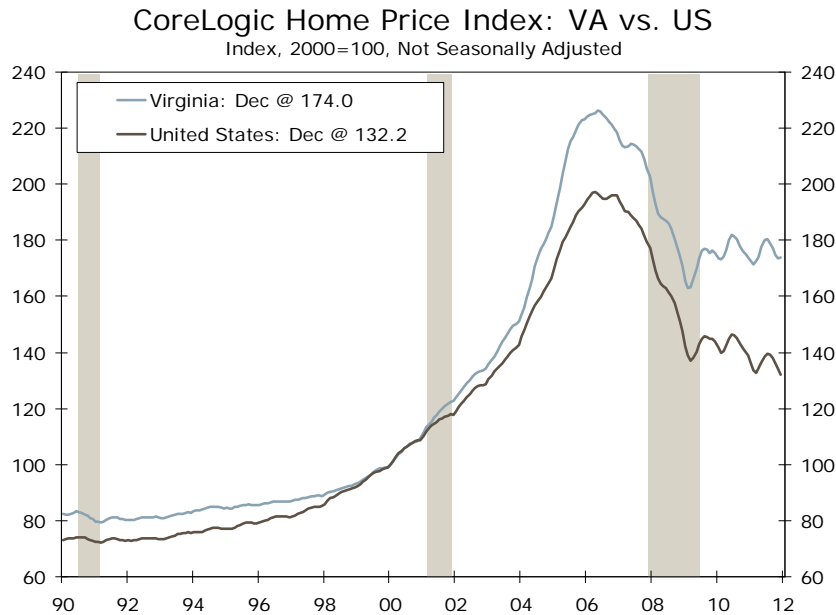


Source: U.S. Department of Commerce and Wells Fargo Securities, LLC

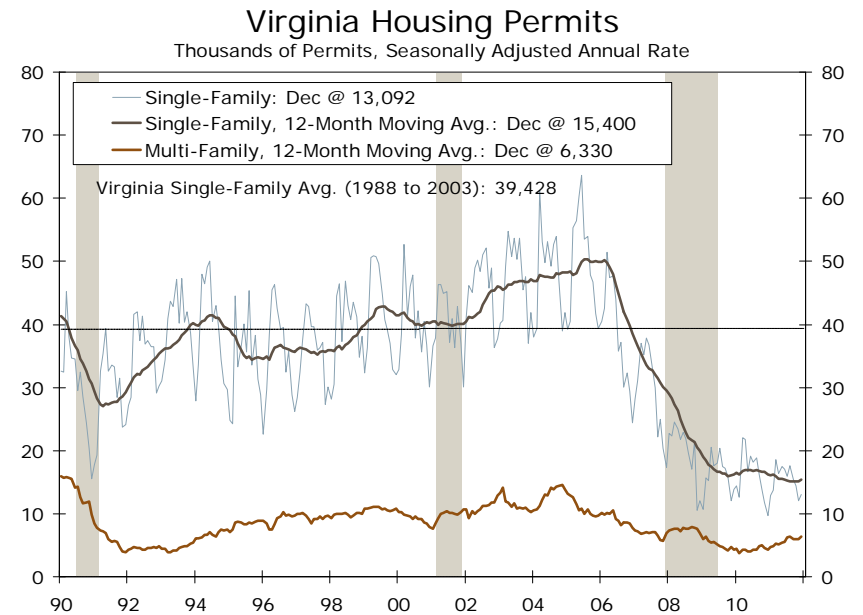
Virginia – Home Prices and Construction

The drop in home prices within the state has been much less severe than the national trend.
Housing construction remains stagnate.

Home Prices



Housing Permits



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

The Norfolk Economy

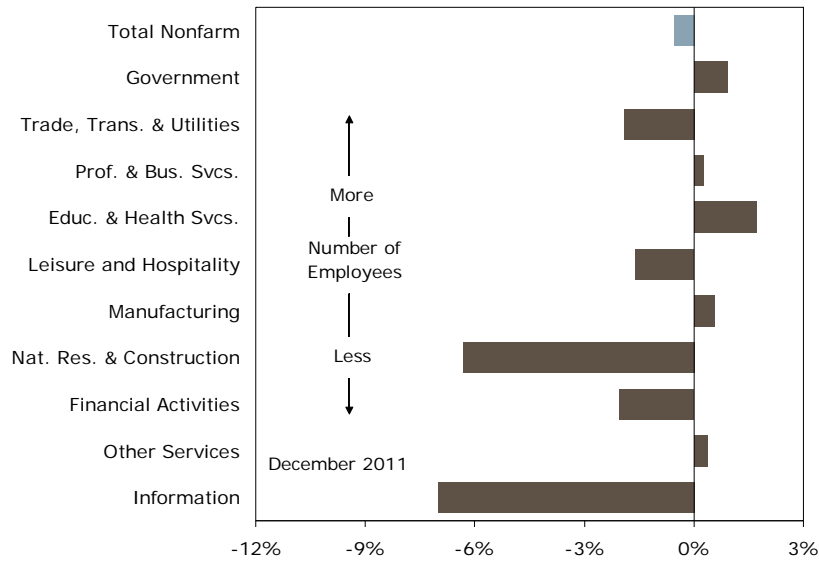
Norfolk – Employment Growth & Unemployment Rate

The labor market in the Norfolk/Hampton Roads area remains weak. Government is a dominant industry in this area, making up 22 percent of the employment base.

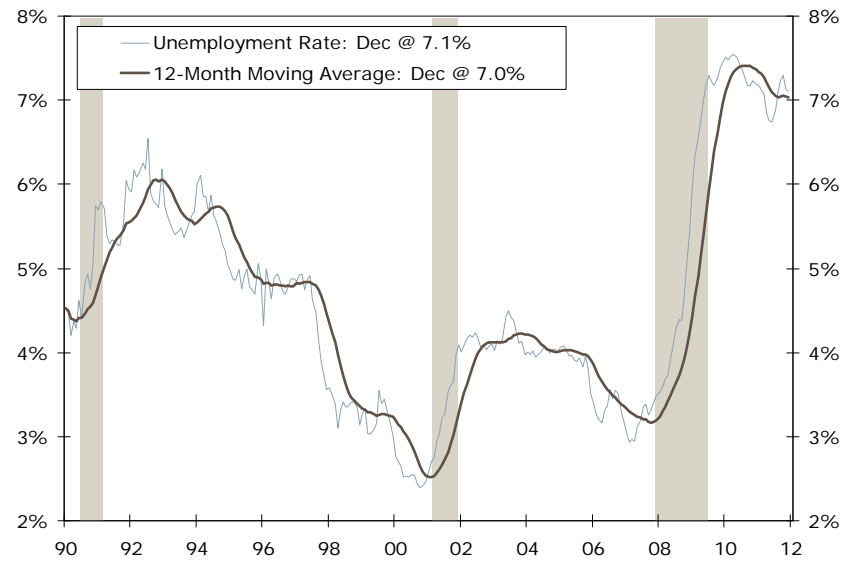
Employment

Unemployment Rate

Va. Beach-Norfolk MSA Employment by Industry
Year-over-Year Percent Change of 3-M Moving Average



Virginia Beach-Norfolk MSA Unemployment Rate
Seasonally Adjusted

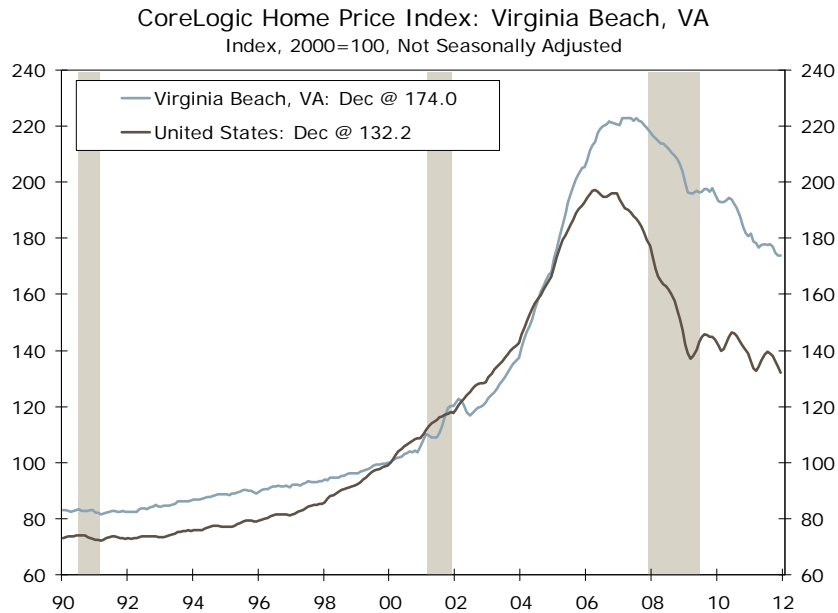


Source: U.S. Department of Labor and Wells Fargo Securities, LLC

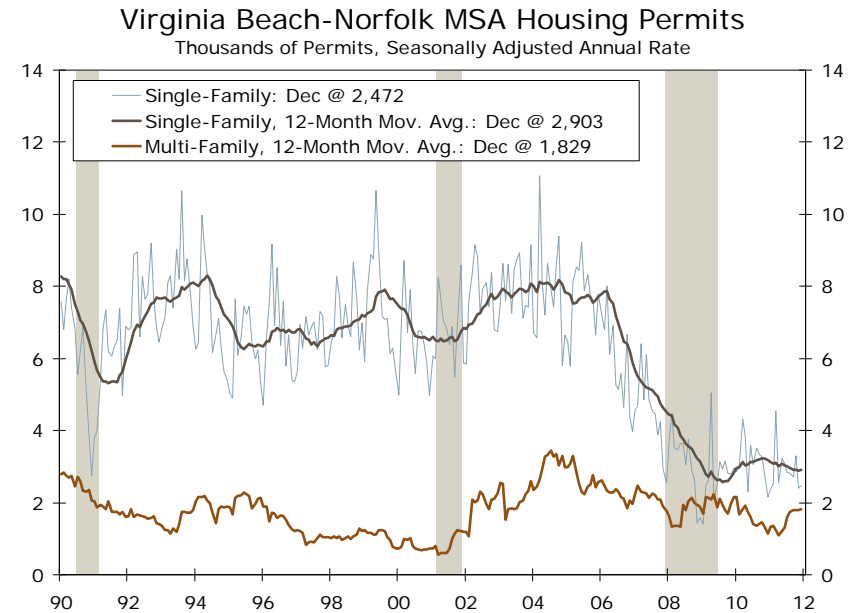
Norfolk – Home Prices and Construction

Local home prices continue to decline due to excess supply.
Modest gains are being made in multifamily construction.

Home Prices



Housing Permits

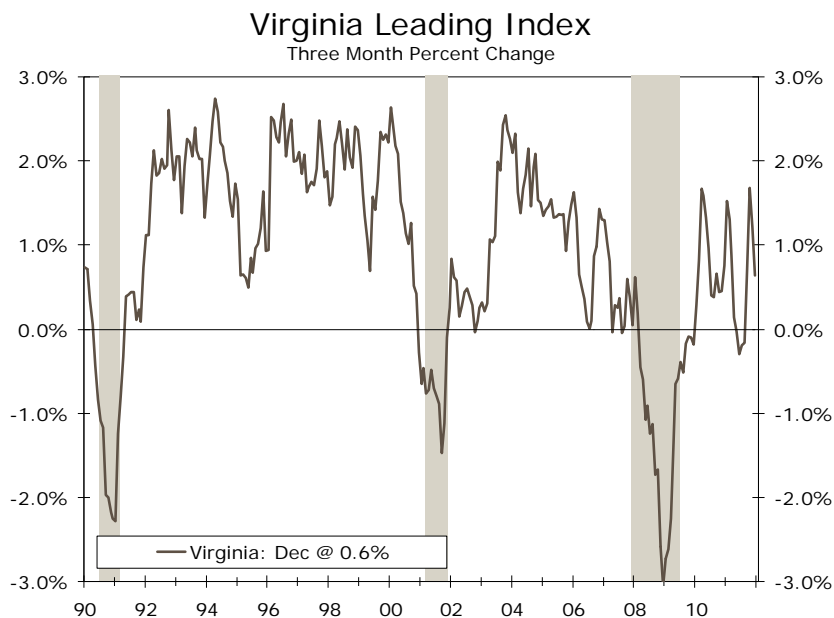


Source: CoreLogic Inc., U.S. Department of Commerce and Wells Fargo Securities, LLC

Virginia & Norfolk – Economic Outlook

The slow pace of economic growth will likely continue, while cuts in federal government spending will weigh on job growth around the state

Leading Index



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

Outlook

- The Virginia economy has been growing at a moderate pace, but the pace appears to be slowing
- The unemployment rate remains far below the national average
 - Job growth will be driven by professional & business services along with the education & healthcare sector
 - Employment growth in the state will be challenging over the next several years due to federal budget cuts
- The housing market continues to be a drag on state's economy

What should we look for in the U.S. economy in the next few quarters?

Expectations for the Future

- A sustained sub-par pace of economic growth
 - More of the same

- Business spending will continue to add to growth
 - Investment in equipment & software will continue

- Consumer spending will remain modest
 - Deleveraging and rebuilding of wealth will continue

- The housing market continues to face many challenges
 - Some regions will recover faster than others

- The employment picture will continue to slowly improve
 - Structural issues remain

Outlook Summary

Wells Fargo U.S. Economic Outlook

	Actual				Forecast	
	<u>2008</u>	<u>2009</u>	<u>2010</u>	<u>2011</u>	<u>2012</u>	<u>2013</u>
Real Gross Domestic Product ¹	-0.4	-3.6	3.0	1.7	1.9	2.1
Personal Consumption	-0.7	-2.0	2.0	2.2	1.7	1.4
Business Fixed Investment	-0.7	-18.0	4.4	8.6	8.8	5.5
Inventory Change	-35.2	-145.0	58.8	35.6	48.5	61.8
Government Purchases	2.5	1.7	0.7	-2.1	-1.9	-1.2
Residential Construction	-23.9	-22.3	-4.3	-1.4	7.4	10.3
Net Exports	-489.7	-358.8	-421.8	-412.4	-432.4	-387.0
Consumer Price Index ²	3.8	-0.3	1.6	3.1	1.9	2.0
Corporate Profits Before Taxes ²	-16.4	9.1	32.2	7.8	6.3	6.6
10-Year Treasury Note	3.66	3.26	3.22	2.78	2.05	2.35

Forecast as of: February 8, 2012

¹ Compound Annual Growth Rate Quarter-over-Quarter

² Year-over-Year Percentage Change

Source: Wells Fargo Securities, LLC

Appendix

A Sampling of Our Recent Special, Regional & Industry Commentary

Recent Special Commentary

Date	Title	Authors
February-08	Bank Lending: Fed's Survey Suggests Support for Growth	Silvia & Watt
February-02	The Fragile Fiscal Policy Outlook: I	Silvia & Brown
January-31	Housing Chartbook: January 2011	Vitner, Khan & Seydl
January-31	How Does The Recent Drop In The Unemployment Rate Square With Okun's Law?	Vitner & Seydl
January-25	FOMC: Why the Recent Past Seldom Predicts the Future	Silvia
January-19	Vacancies and the Housing Recovery	Vitner & Seydl
January-13	How Might Fiscal Restraint Generate Economic Growth?	Silvia & Watt
January-13	Eastern Europe Faces Monetary Policy Dilemma	Anderson & Kashmerek
January-12	Global Chartbook: January 2012	
January-11	Bank Credit: A Surprisingly Typical Cycle	Silvia & Watt
January-05	The Charlotte Economy: Improvement Ahead	Silvia & Brown
December-30	Commodity Price Volatility to Continue	Aleman
December-28	Colorado Outlook: December 2011	Anderson & Kashmerek
December-22	South Korea Moves Forward on Free Trade	Anderson
December-21	Indian Economy: Still Deteriorating at the Margin	Bryson
December-21	Georgia Economic Outlook: December 2011	Vitner & Seydl
December-20	What's Behind the Upward Trend in Housing Activity?	Vitner & Khan
December-14	New Jersey Faces Additional Hurdles	Vitner, Khan & Watt
December-14	Russia: Black Gold and Political Stranglehold	Anderson & Kashmerek
December-20	Arizona: Growth, but at a Lower Gear	Aleman & Swankoski
December-19	Europe in 2012: Renaissance or More Dark Ages	Bryson, Quinlan, & Seydl
December-12	Thunder Down Under: Australia Braces for a Storm	Quinlan
December-09	Pennsylvania Economic Update and Outlook	Bryson, Quinlan, & Seydl
December-08	Minnesota Economic Outlook: December 2011	Anderson & Kashmerek
December-08	Credit Quality Monitor - December 2011	Anderson & Kashmerek
December-05	What is Driving Construction Spending?	Vitner & Khan
November-30	Coordinated Action by Major Central Banks	Bryson
November-30	California Outlook: November 2011	Anderson & Watt
November-22	The Deficit Reduction Committee: A Successful Failure	Silvia, Bullard, Brown & Watt
November-22	Giddy-Up Jingle Horse: Holiday Sales Preview	Vitner, Quinlan, & Seydl
November-16	Global Chartbook: November 2011	
November-15	Has the Fed's Unconventional Approach Been Successful?	Silvia & Khan
November-15	Economic Mobility: Is "Rags to Riches" Still Possible?	Silvia, Quinlan & Seydl
November-14	U.S. States with Exposure to a European Recession	Vitner & Brown
November-07	North Carolina: A Story of Uneven Progress	Silvia & Brown
November-03	Is U.S. Manufacturing in Decline?	Anderson, Brown & Swankoski
November-02	ASEAN-5 Economies Fundamentally Sound	Bryson
November-02	Employment: Beyond the Sound Bites—Reading the Signals IV	Silvia & Watt
November-01	Character of Recovery V: Sector and Employment Differences	Silvia & Iqbal

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