

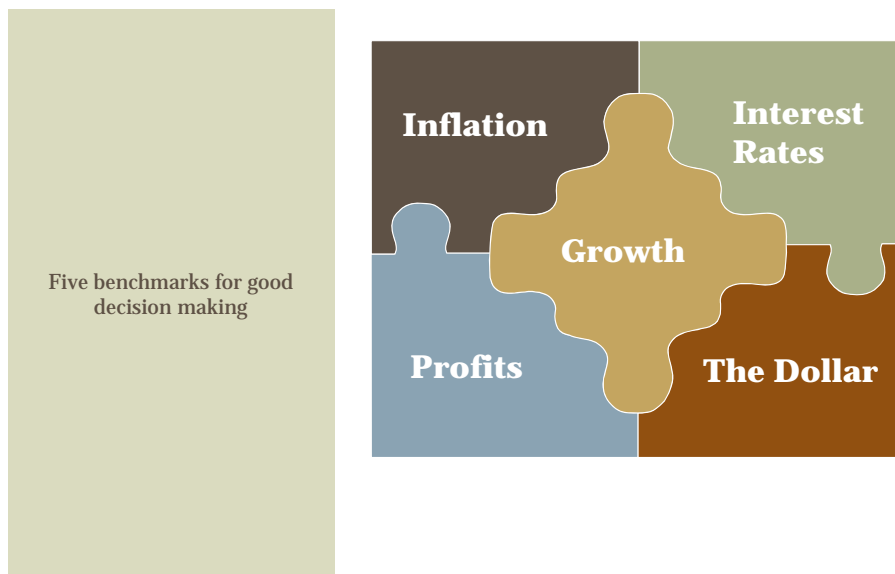


**Economic Outlook: Finance, Housing and the Consumer**  
**Federal Reserve Bank of Chicago Annual Economic Outlook Symposium**

John E. Silvia, Chief Economist  
Friday, December 2, 2011

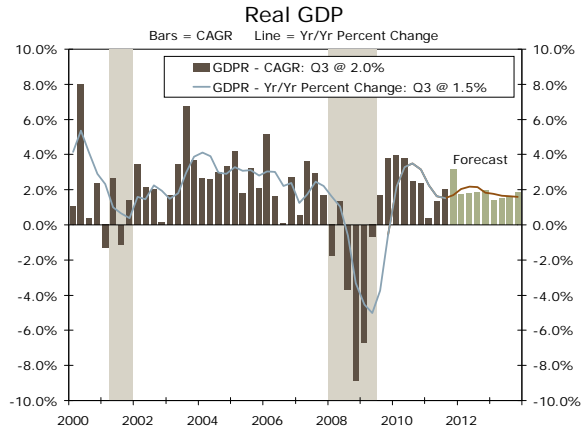


**Where Are We Now?**



What We Get Versus What We Expect

Sustained recovery in 2012, but still below historical experience

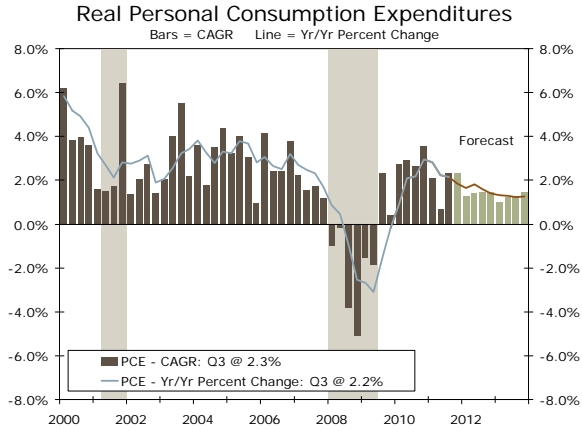


Source: U.S. Department of Commerce and Wells Fargo Securities, LLC

Consumers: Better Returns, Fewer Players

Consumer Spending

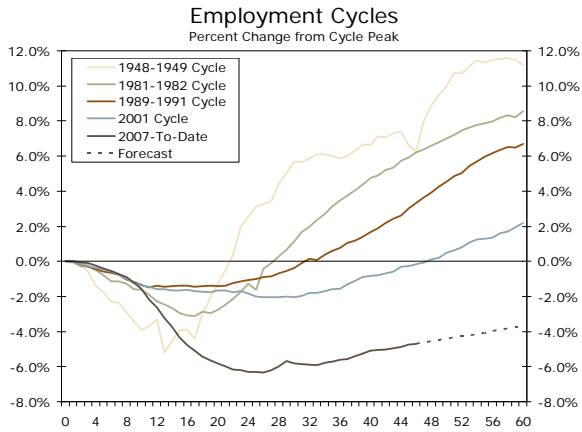
Subpar recovery suggests deleveraging consumer, cautious credit and slow job gains



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

Employment

Employment will eventually regain its peak, but not quickly

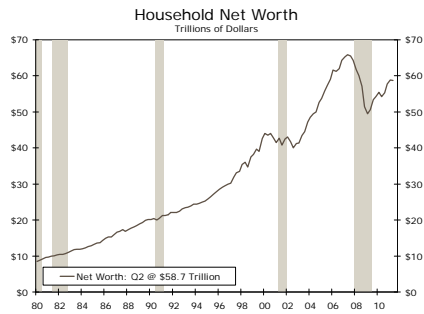


Source: U.S. Department of Labor and Wells Fargo Securities, LLC

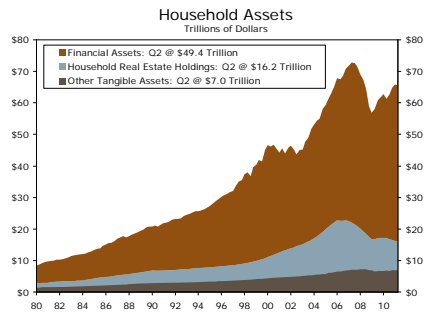
**Household Wealth**

Wealth has rebounded since the recession, driven by gains in financial markets

**Total**



**Composition**

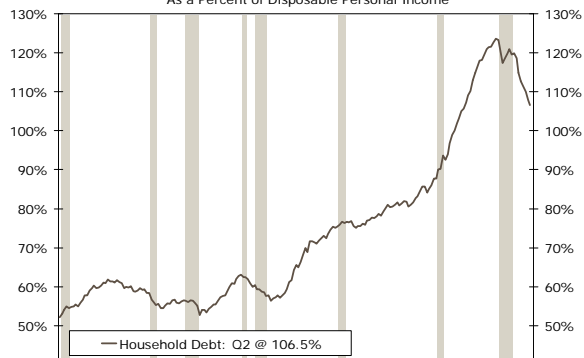


Source: Federal Reserve Board and Wells Fargo Securities, LLC

**Household Finances**

Consumers are reducing their debt, but leverage remains historically high

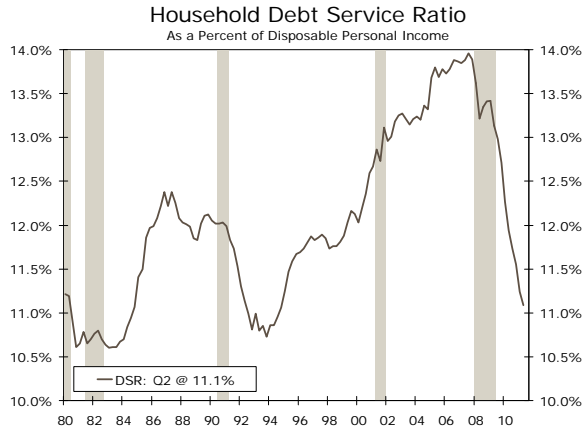
**Household Debt - Consumer & Mortgage**  
As a Percent of Disposable Personal Income



Source: Federal Reserve Board and Wells Fargo Securities, LLC

Household Finances: Current Income

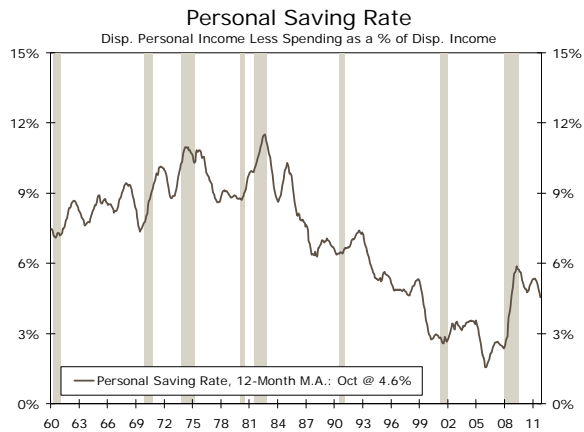
Debt service has returned to more sustainable rates



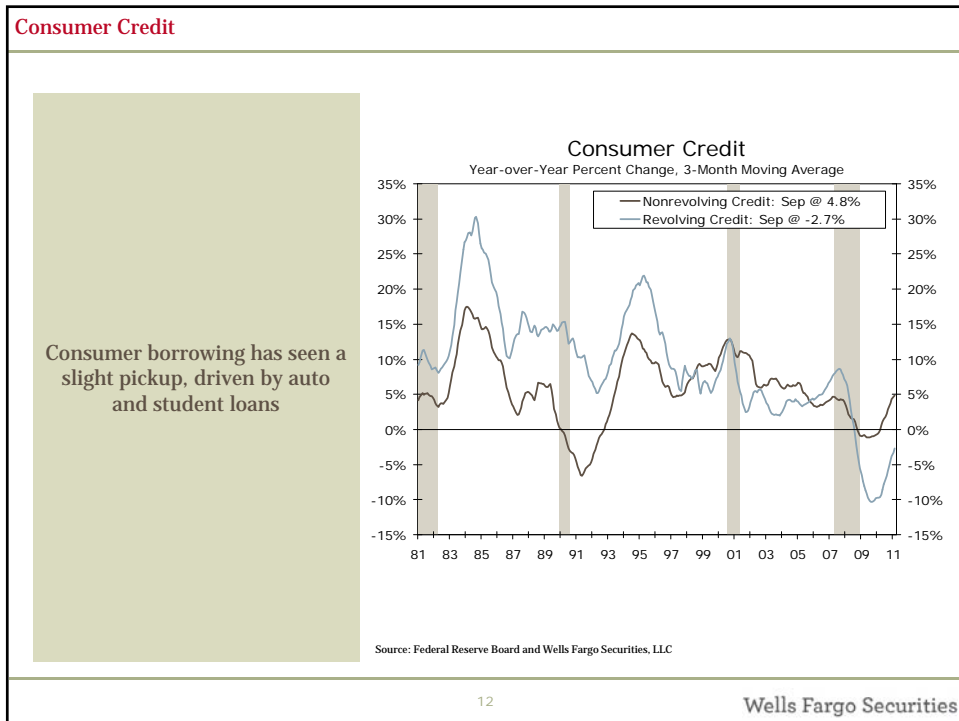
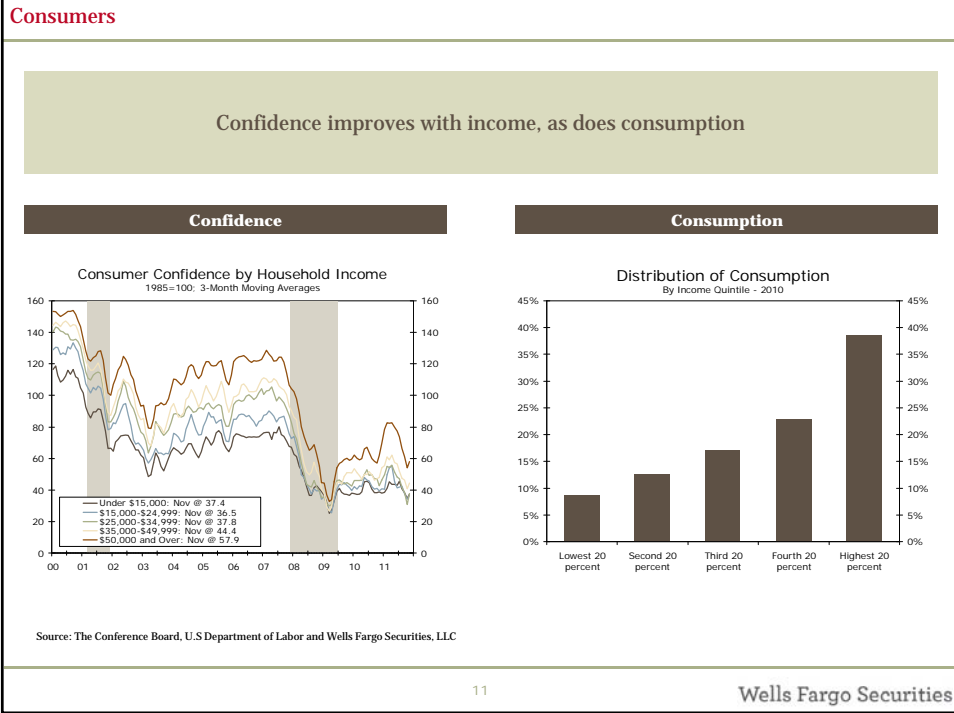
Source: Federal Reserve Board and Wells Fargo Securities, LLC

Household Finances

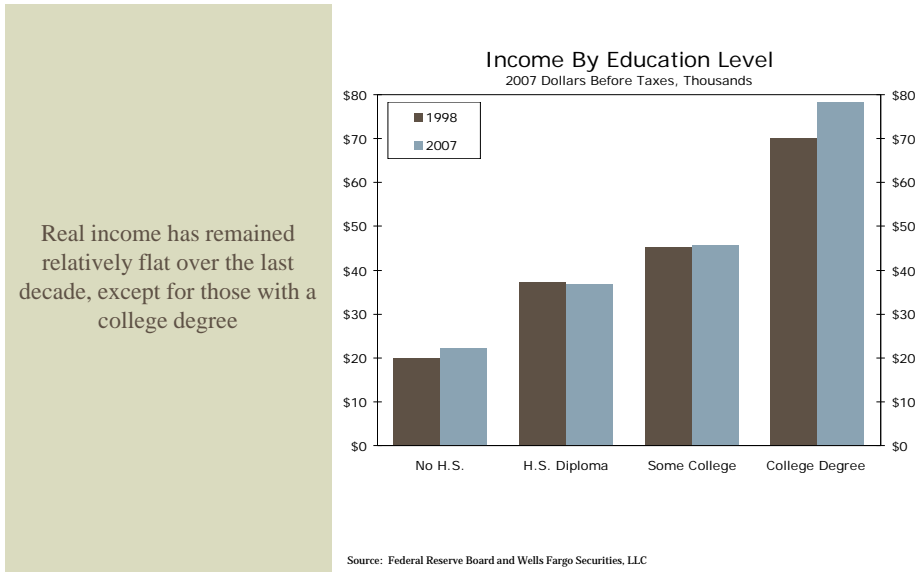
Consumers are saving at higher rates after the last economic shock



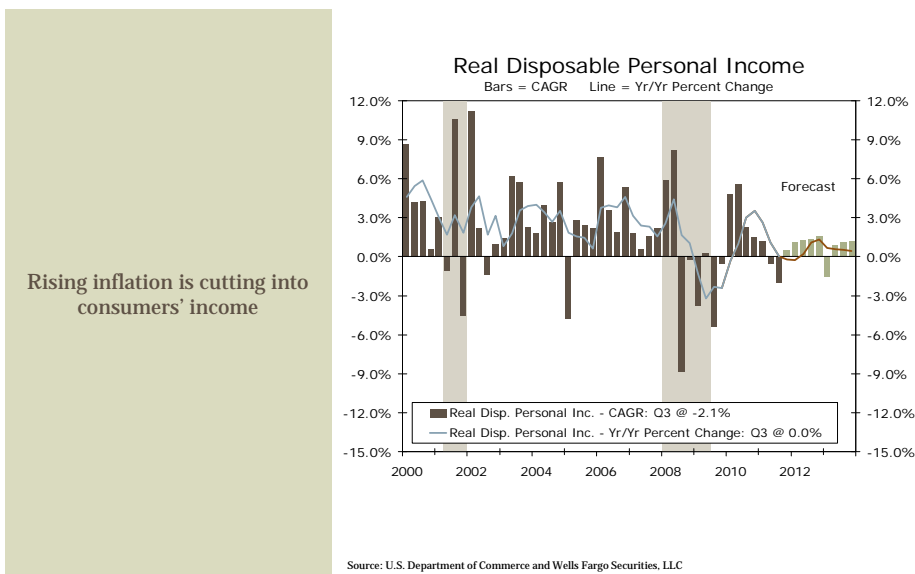
Source: U.S. Department of Commerce and Wells Fargo Securities, LLC



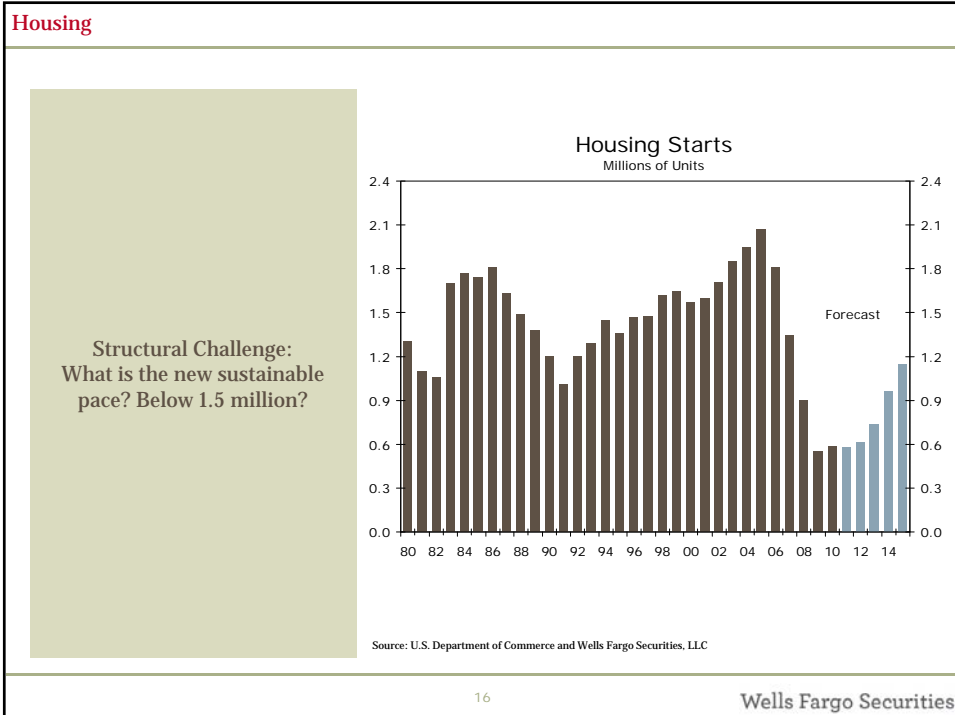
**Income: Rising Returns to Education**



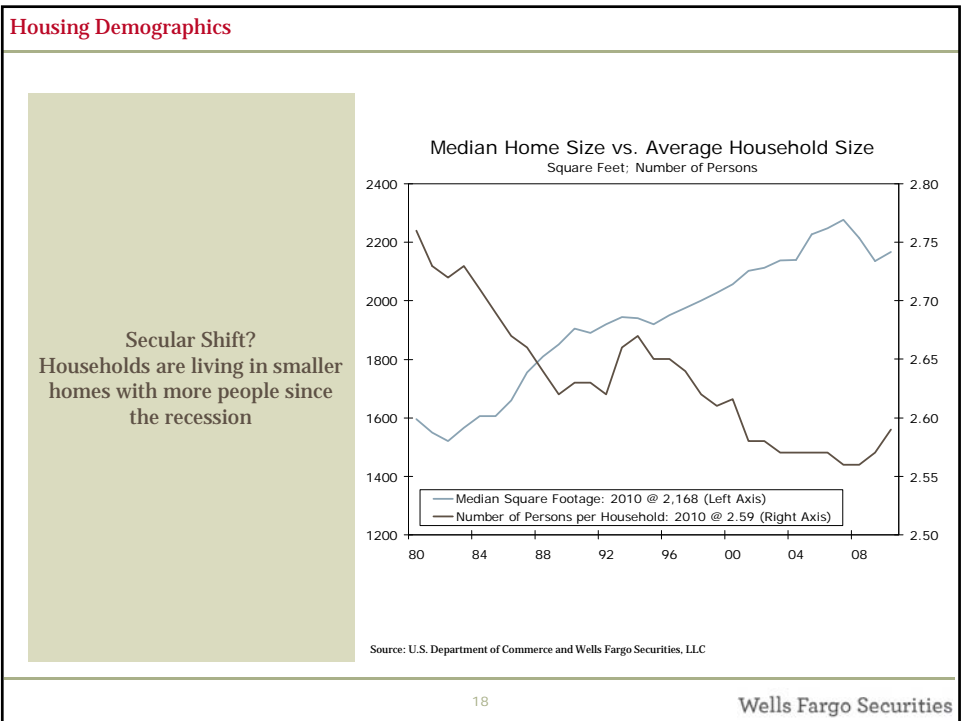
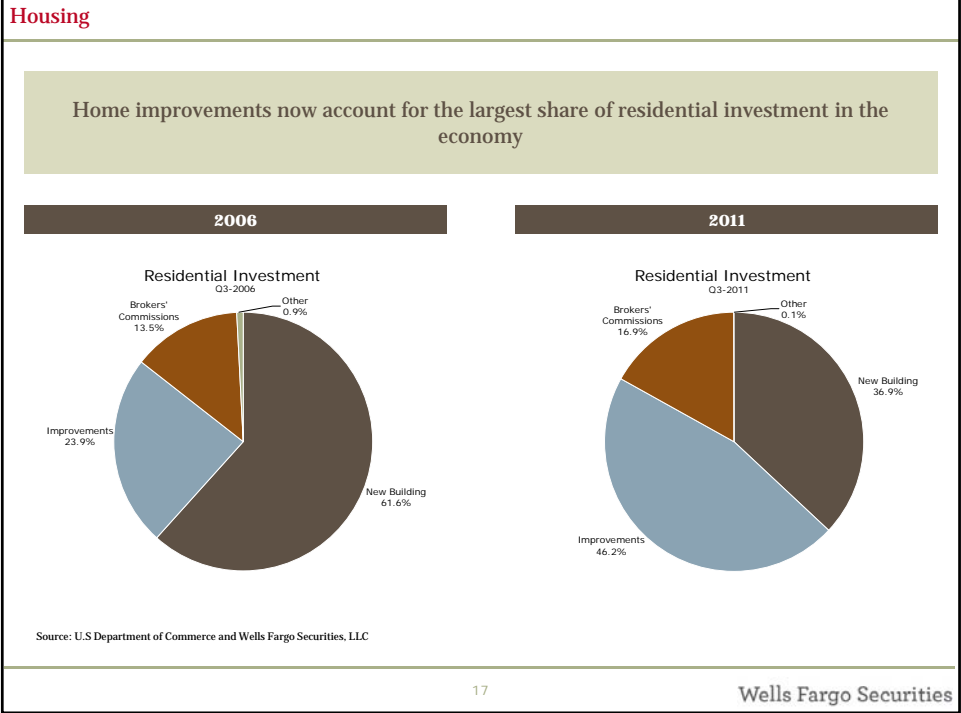
**Personal Income**



## Housing: Poor Returns, Fewer Players

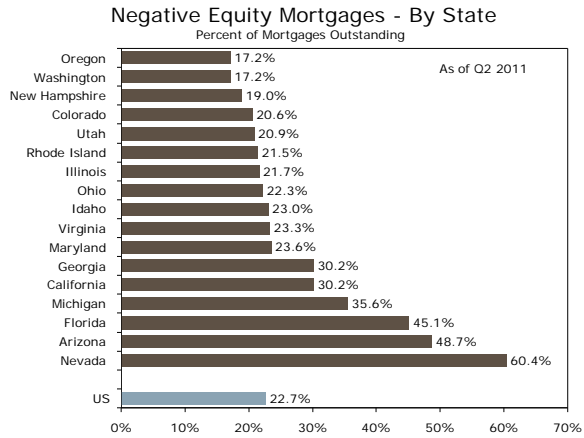






Housing

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

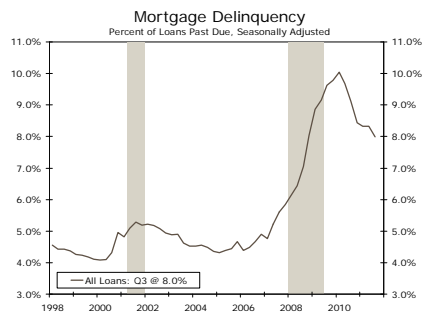


Source: CoreLogic and Wells Fargo Securities, LLC

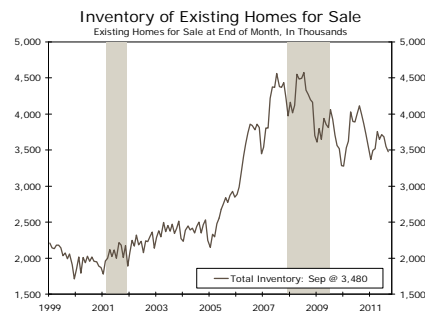
Housing

Delinquencies and inventories have come down somewhat from their all-time peaks, but still remain elevated

Delinquencies



Inventory



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

**Home Prices: Temporary Actions Do Not Provide Permanent Change**

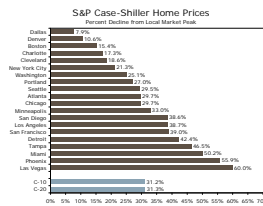
Timing of Recovery Will Vary Across Metro Areas

**S&P/Case-Shiller Home Price Index – September**

	<u>Yr/Yr % Change</u>	<u>3-Month Annual Rate</u>
Charlotte	-2.55%	-3.45%
Dallas	-0.80%	3.09%
Los Angeles	-4.20%	-9.50%
San Francisco	-5.91%	-9.64%
New York City	-2.63%	2.37%
Washington, DC	0.91%	6.95%

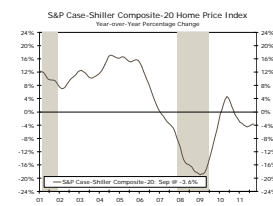
The steepest declines are behind us, but recovery will be slow in areas with excess supply

**Historical Perspective**



Source: S&P Case-Shiller and Wells Fargo Securities, LLC

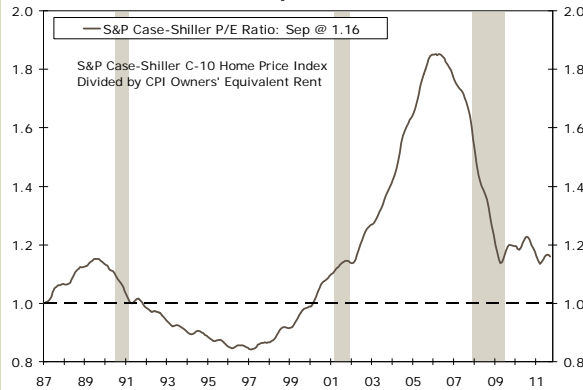
**Historical Perspective**



**Home Prices**

The cost of ownership versus renting has returned to more sustainable levels

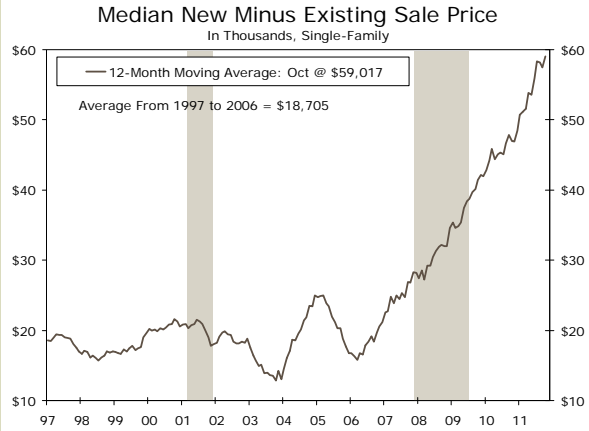
**S&P Case-Shiller Home Price Index P/E Ratio**  
January 1987=100



Source: S&P Case-Shiller, U.S. Department of Labor and Wells Fargo Securities, LLC

Housing

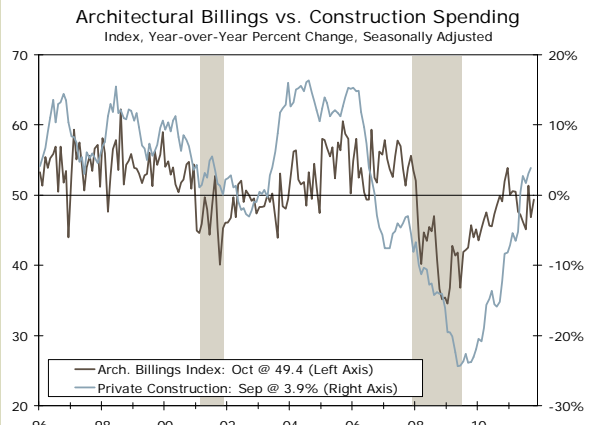
Falling prices of existing homes make them more attractive to new construction



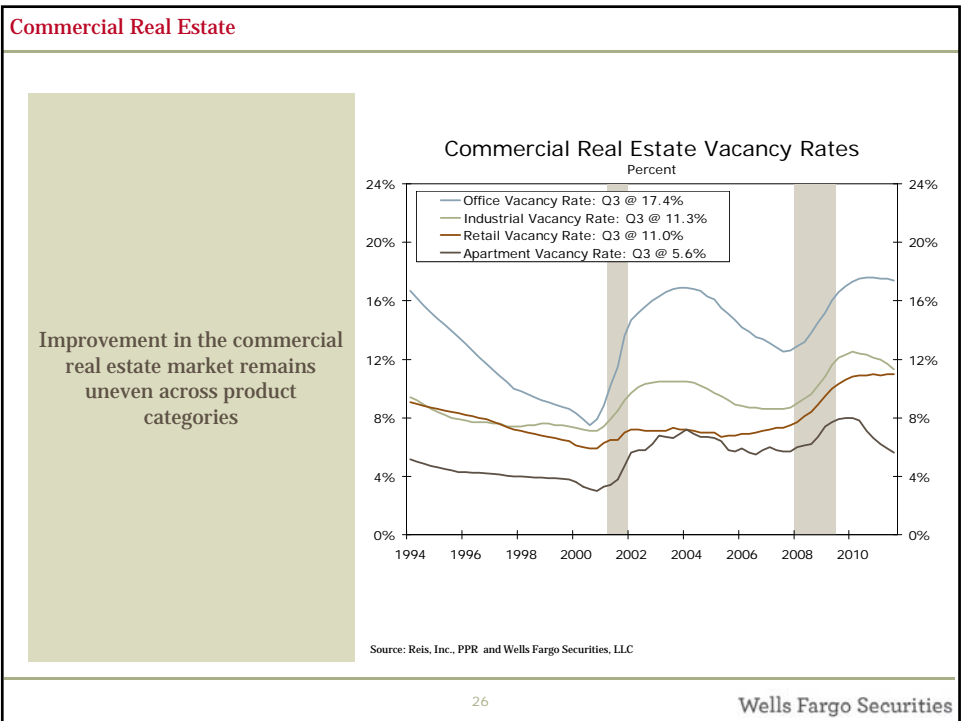
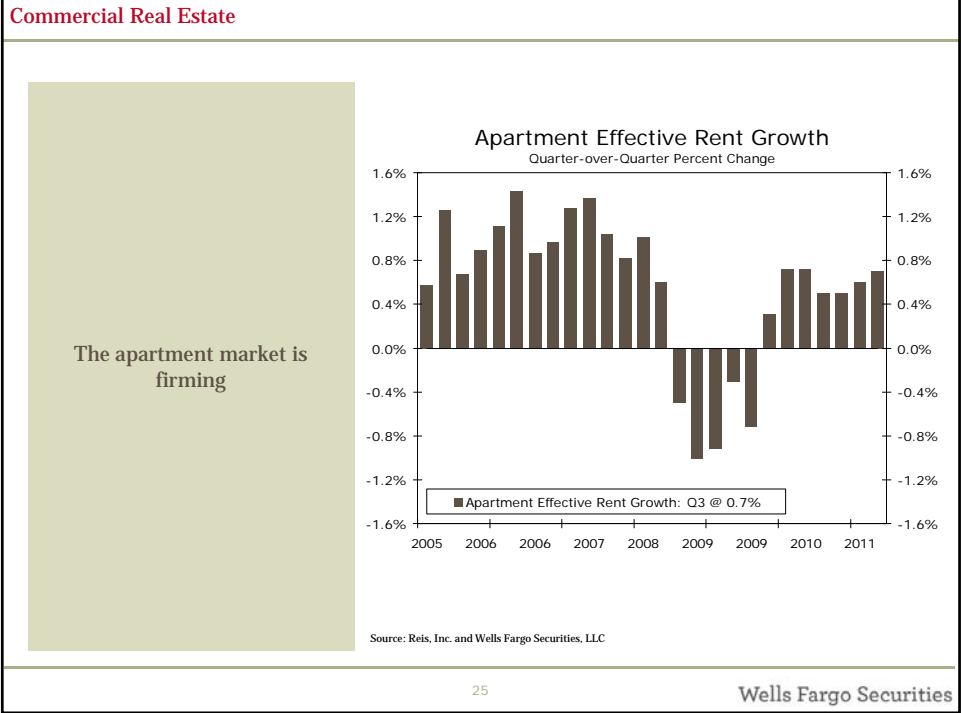
Source: U.S. Department of Commerce, National Association of Realtors and Wells Fargo Securities, LLC

Commercial Real Estate

Typical Cyclical Pattern:  
Commercial and industrial billings has gained momentum due to increased activity in the manufacturing sector



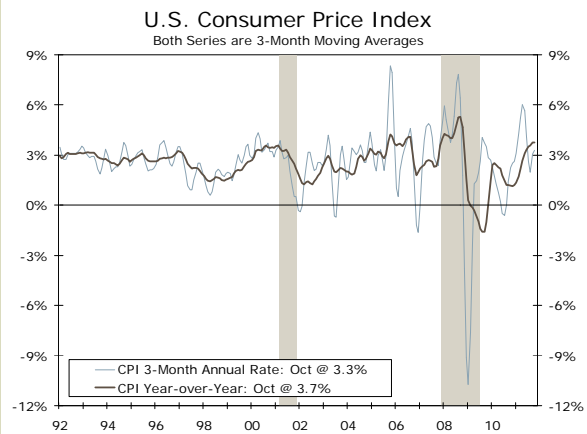
Source: The American Institute of Architects, U.S. Department of Commerce and Wells Fargo Securities, LLC



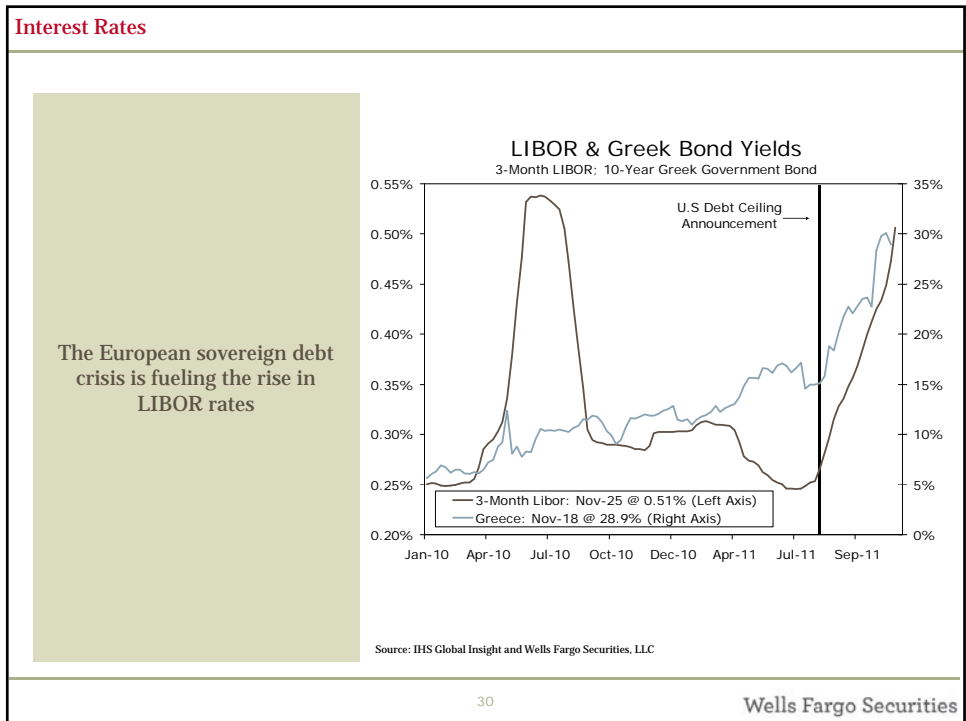
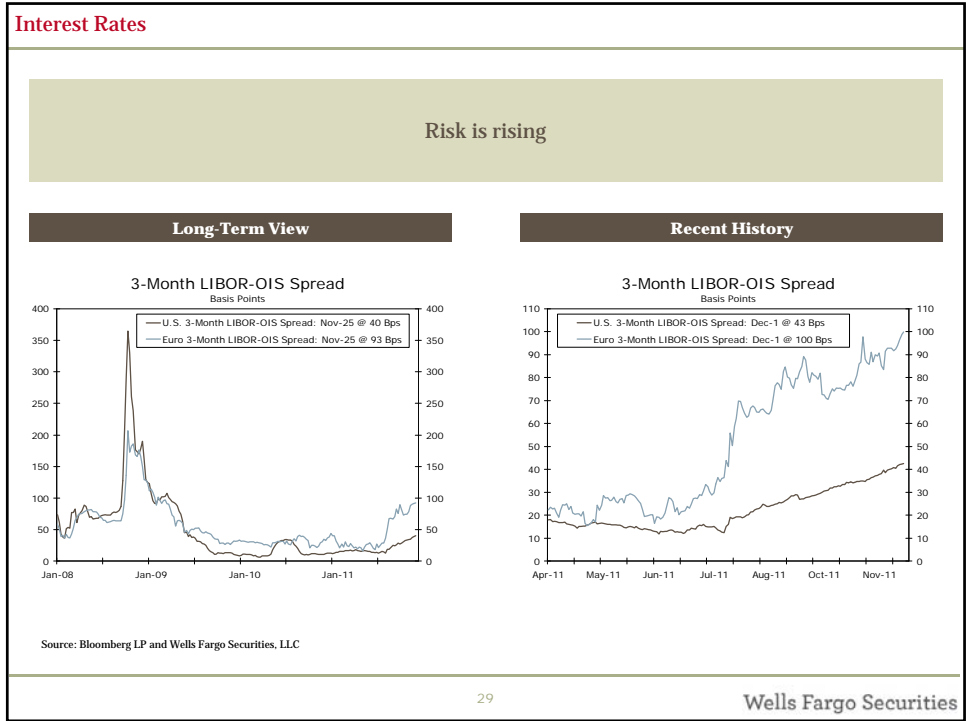
## Financial: Weaker Returns, Many Players

### Inflation

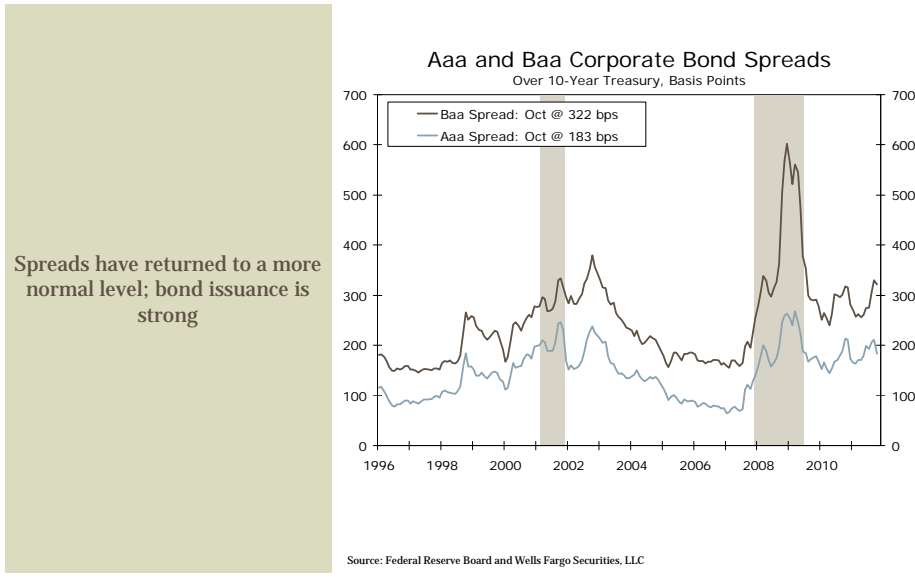
Consumer prices are beginning to pick up on the heels of higher food and housing prices



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



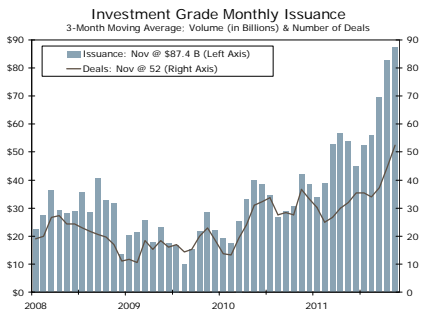
**Corporate Spreads: Positive for Issuance**



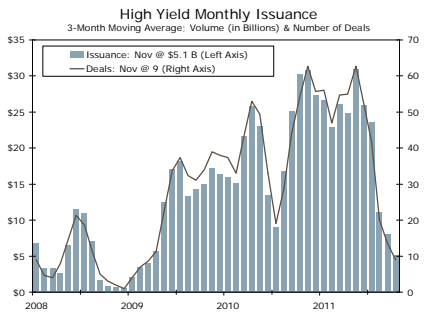
**Debt Issuance: A New Mix**

Issuance has swung away from riskier debt

**High Grade**



**High Yield**

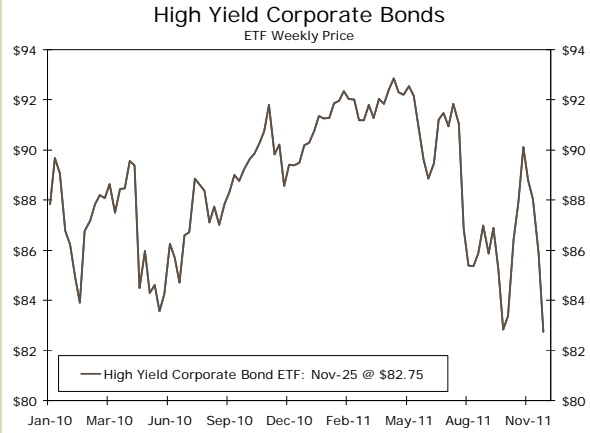


Source: Wells Fargo Securities, LLC



High Yield Assets

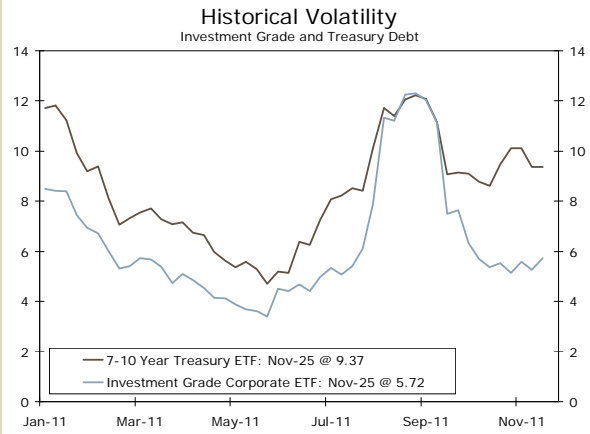
The recent rally in risk assets was short lived



Source: Bloomberg LP and Wells Fargo Securities, LLC

Volatility

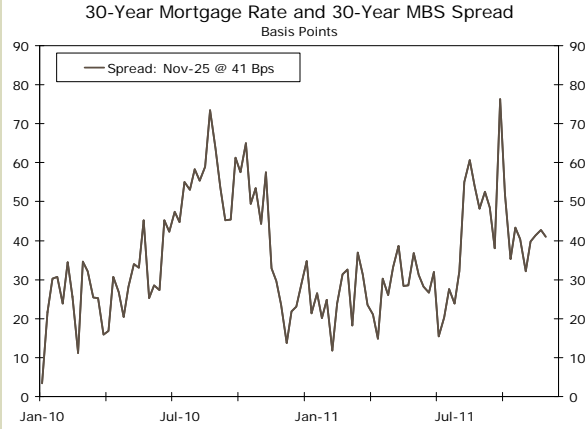
Volatility in Treasury debt continues



Source: Bloomberg LP and Wells Fargo Securities, LLC

**Mortgage Origination**

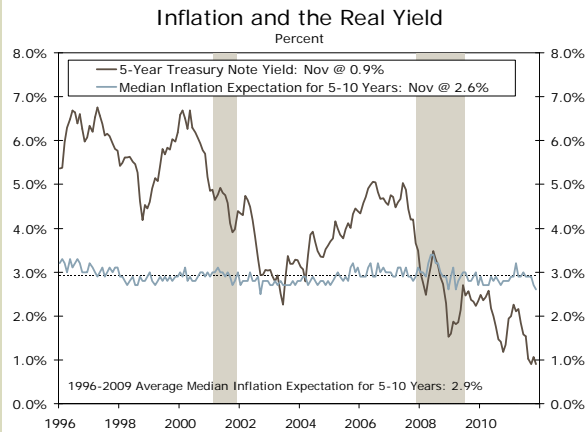
The appetite and capacity for mortgage originations in the banking sector are outside the Fed's control



Source: Freddie Mac, Bloomberg LP and Wells Fargo Securities, LLC

**Inflation vs. Yields: Negative Real Yields, Three Non-Market Buyers**

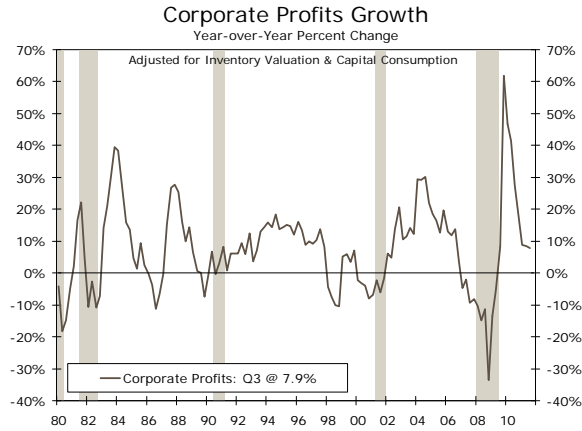
Inflation expectations exceed nominal returns



Source: Federal Reserve Board and Wells Fargo Securities, LLC

Corporate Profits: Global Growth

Profits growth has moderated—  
typical cyclical pattern



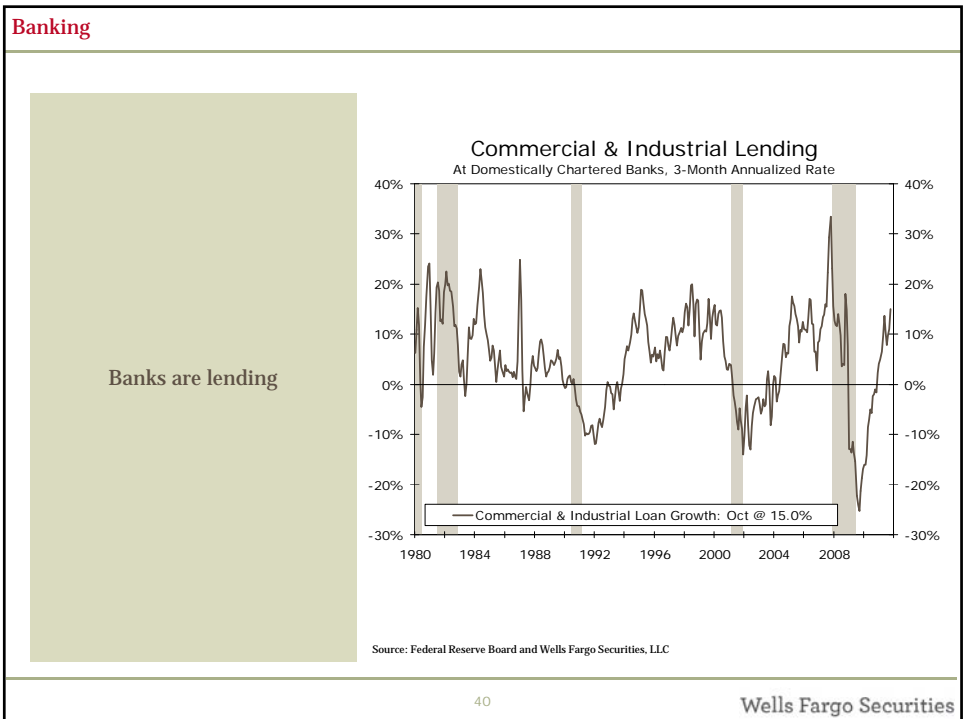
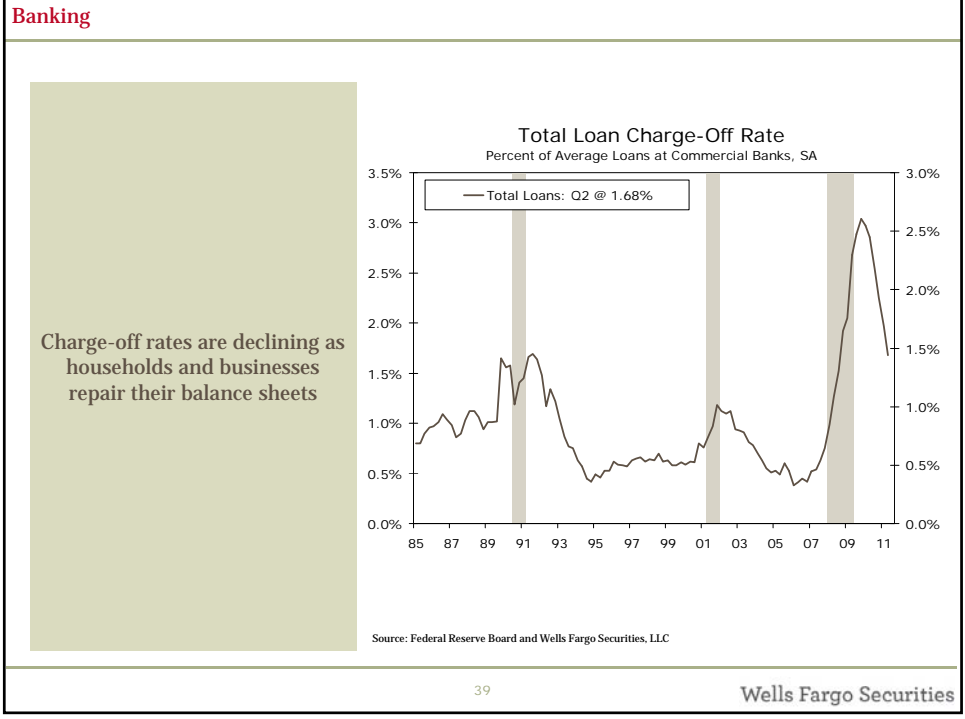
Source: U.S. Department of Commerce and Wells Fargo Securities, LLC

Corporate Profits

A significant portion of profits  
are being earned abroad

Globalization and Corporate Profits	
Sector	Percentage of Total Sales Earned
	Abroad (07-09 Average)
Information Technology	56.9%
Energy	48.1%
Materials	44.9%
Industrials	36.7%
Consumer Staples	27.5%
Consumer Discretionary	24.0%
Financials	18.0%
Health Care	17.4%
Telecommunications	0.6%

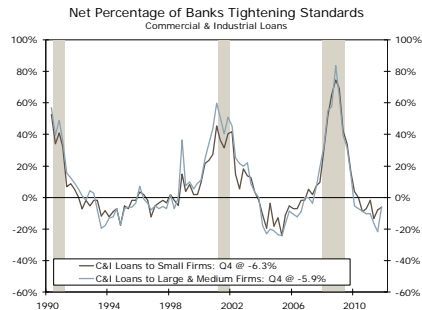
Source: Factset and Wells Fargo Securities, LLC



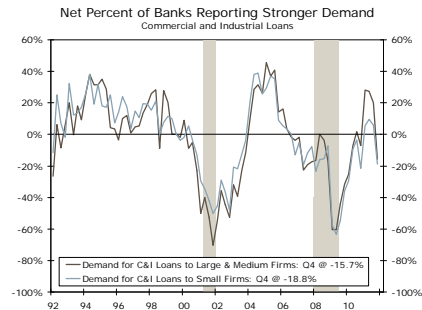
**Banking**

Standards are being relaxed, but demand for loans has fallen sharply in recent months

**Standards**



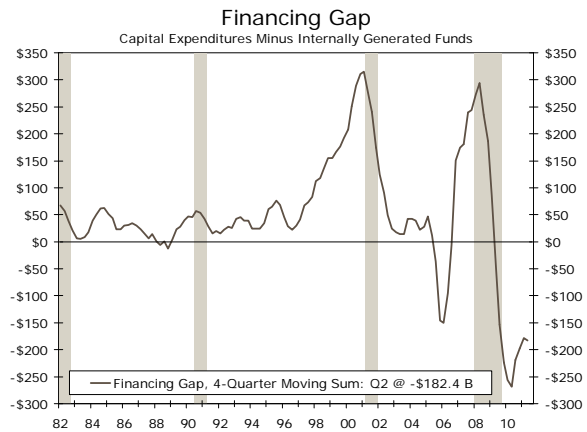
**Demand**



Source: Federal Reserve Board and Wells Fargo Securities, LLC

**Financing Gap**

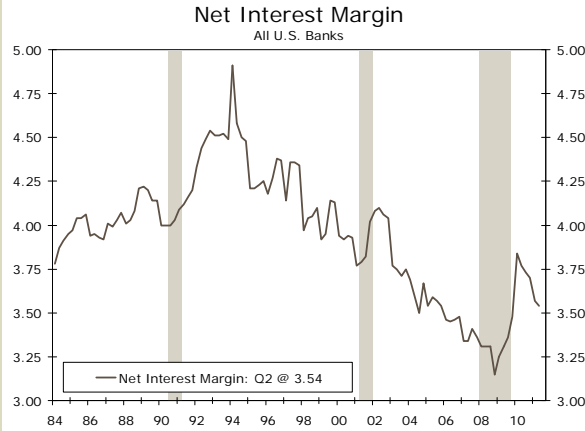
Many companies are currently able to fund their own capital expenditures



Source: Federal Reserve Board and Wells Fargo Securities, LLC

**Banking Interest Margins**

The initial boost to margins from a low fed funds target rate is fading

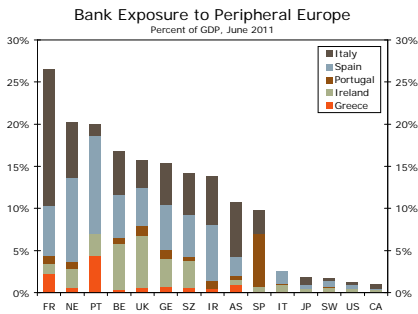


Source: Federal Financial Institutions Examination Council and Wells Fargo Securities, LLC

**Banking**

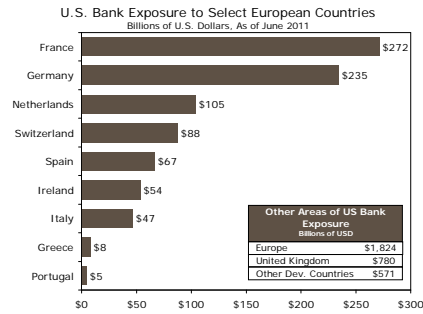
U.S. banks have relatively little bank exposure to the European periphery

**Country Exposure to Europe**



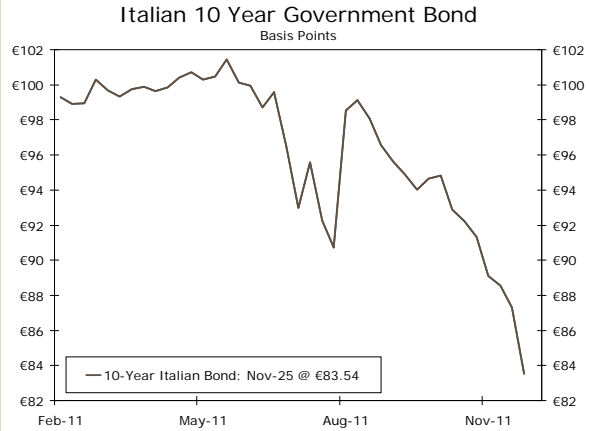
Source: Bank for International Settlements and Wells Fargo Securities, LLC

**U.S. Exposure to Europe**



European Sovereign Debt

Italian bond prices are under pressure

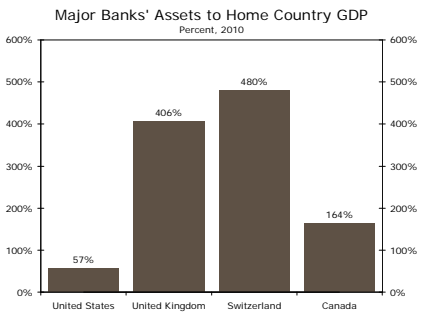


Source: Bloomberg LP and Wells Fargo Securities, LLC

Banking: Assets to GDP

Size is a relative matter

Country



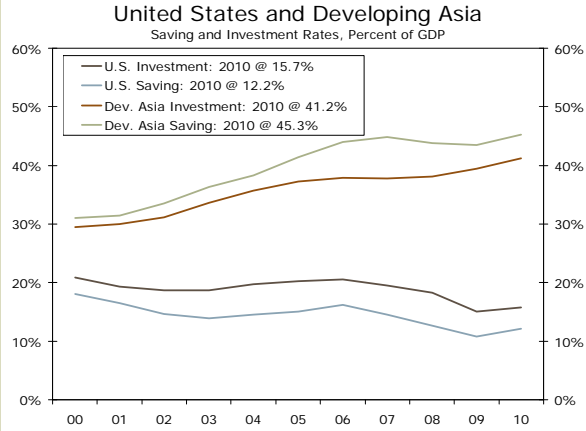
Source: SNL Financial LC, IMF and Wells Fargo Securities, LLC

Institution

Institution	Total Assets (Billions)	Country	Assets to GDP
Bank of America Corporation	2,265	United States	15%
JPMorgan Chase & Co.	2,118	United States	14%
Citigroup Inc.	1,914	United States	13%
Wells Fargo & Company	1,258	United States	9%
U.S. Bancorp	308	United States	2%
PNC Financial Services Group, Inc.	264	United States	2%
Bank of New York Mellon Corporation	247	United States	2%
Royal Bank of Canada	713	Canada	45%
Toronto-Dominion Bank	608	Canada	39%
Bank of Nova Scotia	517	Canada	33%
BMO Financial Group	404	Canada	26%
Canadian Imperial Bank of Commerce	345	Canada	22%
HSBC Holdings Plc	2,455	United Kingdom	109%
Barclays Plc	2,333	United Kingdom	104%
Royal Bank of Scotland Group Plc	2,276	United Kingdom	101%
Lloyds Banking Group Plc	1,554	United Kingdom	69%
Standard Chartered Plc	517	United Kingdom	23%
UBS AG	1,411	Switzerland	269%
Credit Suisse Group AG	1,105	Switzerland	211%

U.S. and Developing Asia

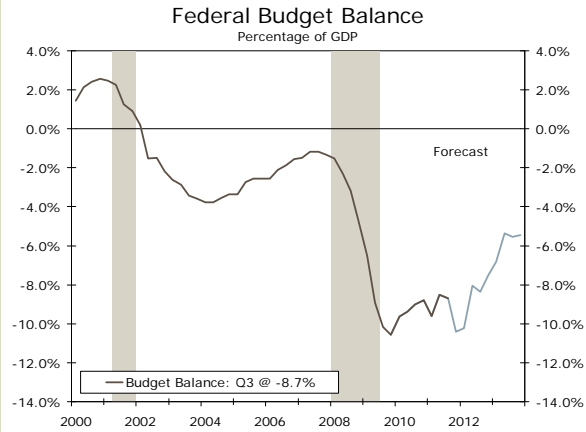
High saving/investment rates in Asia should continue to underpin strong economic growth for the foreseeable future



Source: International Monetary Funds and Wells Fargo Securities, LLC

Difficult Choices

The nation has entered uncharted waters in fiscal policy



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



Outlook Summary

Wells Fargo U.S. Economic Outlook

	Actual			Forecas	
	2008	2009	2010	2011	2012
Real Gross Domestic Product <sup>1</sup>	-0.4	-3.6	3.0	1.8	2.0
Personal Consumption	-0.7	-2.0	2.0	2.3	1.6
Equipment and Software	-4.1	-16.4	14.6	10.4	8.5
Government Purchases	2.5	1.7	0.7	-1.9	-1.1
Consumer Price Index <sup>2</sup>	3.8	-0.3	1.6	3.2	2.0
Corporate Profits Before Taxes <sup>2</sup>	-16.4	7.9	32.2	7.9	6.3
10-Year Treasury Note	3.66	3.26	3.22	2.67	2.28

Forecast as of: November 22, 2011

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

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

Source: U.S. Department of Commerce, U.S. Department of Labor, Federal Reserve Board and Wells Fargo Securities, LLC

Appendix

**Wells Fargo Economics Group Publications**

**A Sampling of Our Recent Special, Regional & Industry Commentary**

To join any of our research distribution lists please visit our website:  
<http://www.wellsfargo.com/economics>

**Recent Special Commentary**

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
October-25	Regional Chartbook: Quarter 4, 2011	Vitner, Brown & Seydl
October-11	Employment: Beyond the Sound Bites—Reading the Signals V	Silvia & Watt
October-06	Real Home Prices: A Midno-Area Look	Vitner & Seydl
October-03	More QE from the Fed?	Bryson
September-28	Economic Dynamism in Southeast Asia	Silvia
September-27	Ireland: Good News from the European Periphery?	Bryson
September-27	Independent Nations, Interdependent Economies	Silvia
September-26	Employment: Beyond the Sound Bites—Reading the Signals IV	Silvia & Watt
September-21	"Operation Twist" Gets Underway	Bryson
September-20	Credit Quality Monitor: September 2011	Anderson & Kashmarek
September-16	Global Chartbook: September 2011	
September-15	Florida Economic Outlook: September 2011	Vitner, Brown & Seydl
September-09	The Direction of Treasury Rates: A Japanese Story?	Anderson, Bryson & Seydl
September-08	Long-Term Unemployment: Costs & Consequences	Silvia & Watt
September-07	Housing Data Wrap-Up: September 2011	Vitner, Khan & Seydl
September-07	Brazil: GDP and Central Bank Autonomy	Albram
September-06	Strength of Currency Weights on Swiss GDP Growth	Bryson
September-02	Is Another Recession Brewing in Germany?	Bryson & Kruse
September-01	Housing and Autos: Rebuilding a Marketplace	Aleman & Kruse
August-30	The Evolution of Economic Relationships: The PMI and Growth	Silvia, Iqbal & Watt
August-26	Tacking in Treacherous Water: No Full Sail for QE3	Silvia
August-26	Brazilian Economy: Growing Pains	Albram
August-24	Will the Remnant Eventually Reveal the Dollar?	Bryson
August-23	State Coincident Indicators Highlight A Disturbing Trend	Vitner & Brown
August-23	Are We Headed for Another Global Recession?	Bryson, Quinlan & Kruse
August-22	Philadelphia Fed Index: Can It Predict a Recession?	Silvia, Khan, Iqbal & Watt
August-22	Gold Bubble Fears Overblown	Anderson & Kashmarek
August-22	Mexican Economy Grows Despite Slowdown in Q2	Albram
August-22	The Kids Are Alright	Silvia, Quinlan & Seydl
August-19	Even Slower Growth with Significant Downside Risk	Silvia
August-15	Why is France in the Crosshairs?	Bryson & Kruse
August-11	Commercial Real Estate Chartbook: Quarter 2	Vitner, Khan & Seydl
August-11	Employment: Beyond the Sound Bites—Reading the Signals III	Silvia & Watt
August-07	SAP Downgrade of Treasury /Fed Credit: Fiscal Imbalances	Silvia & Vitner
August-06	What are the Risks of Recession?	Vitner
August-02	Economic Implications of the Debt Ceiling Compromise	Silvia, Vitner, Bullard & Brown
August-02	Real GDP Per Capita Stalled Out In the First Half of 2011	Vitner & Seydl
August-01	Employment: Beyond the Sound Bites—Reading the Signals II	Silvia & Watt

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