

Global Weekly Flash

Madrid, 1 March 2013
Economic Analysis

Financial Scenarios

Cristina Varela Donoso
cvarela@bbva.com
+34 91 537 7825

María Martínez Álvarez
maria.martinez.alvarez@bbva.com
+34 91 537 66 83

Alejandro Neut
robertoalejandro.neut@bbva.com

Ignacio Santiago Llorente
i.santiago.llorente@bbva.com
+34 91 537 76 80

Indicators collaboration:

Europe
Agustín García
agustin.garcia@bbva.com
+34 537 79 36

US
Alejandro Vargas
alejandro.vargas@bbvacompass.com
+1 713 831 7348

Asia
Fielding Chen
fielding.chen@bbva.com.hk
+852 2582 3297

Central Banks supportive amidst political uncertainties and a still fragile recovery

Early this week, European financial markets were rattled by the results of Italy's elections. The Italian 10Y yield increased by 29%, and the euro fell below 1.30 against the US dollar, its lowest level in two months. However, the Italian Treasury found enough demand to issue long-term debt (although at a higher borrowing cost). By the end of the week, contagion to Spain and others peripherals was softer than expected; the 10Y Spanish yield decreased by 7bps in the week. But uncertainties are likely to remain high for now as a grand coalition in Italy seems to be difficult achieve. Furthermore, according to several news sources, it seems that the US 'sequester' will not be avoided. The full implementation of the spending will significantly weigh on US GDP growth in 2013. Flows toward safe-haven assets increased this week, especially in the eurozone. The German 10Y bond yield fell by 12 pbs and the 2Y yield decreased by 9 bps. In the US, drops in government yields were lower, of around 11 bps the 10Y bonds. Against this backdrop, Central Banks are expected to remain supportive.

- In the Italian elections held last Sunday and Monday, Bersani's centre-left coalition (the favorite in the polls) won by a very small margin of the votes with respect to Berlusconi's centre-right in the Chamber of Deputies, which led automatically to majority of seats. However, he failed to secure a majority in the Senate, implying a hung Parliament and increasing political uncertainty in Italy. On 15 March the new Italian parliament is expected to convene. Several political scenarios may emerge, ranging from new elections to a grand coalition. Media reports suggest that a grand coalition scenario will not be easy to achieve, while chances for a minority government are growing, which may increase volatility in European debt markets.
- Despite the Italian deadlock, the Italian Treasury managed to sell EUR 6.5bn in long-term debt. Bid-to-cover ratios grew slightly higher than in previous auctions, increasing to 1.6x from 1.3x in the previous auction of the 10Y bond reference. Borrowing costs surged but remained below pre-auction yields in secondary markets. European banks did not shift their liquidity provisions. At this week's ECB's liquidity auctions, Eurozone banks renewed EUR 132bn in 7-day MROs and 8bn in 3M LTROs, almost the same amount that matured.
- Contagion from Italy to Spain was initially large, but it has faded over the week. The announcement of the reduction in 2012's public deficit together with the correction of the current account deficit helped Spain to decouple from tensions in Italy. According to the Spanish government, the public deficit ended 2012 at 6.7% of GDP, excluding the funds for bank recapitalization. The reduction of the deficit of the Autonomous regions was particularly noticeable. Next week ministers will discuss at the Eurogroup meeting, among other issues, the Excessive Deficit Procedure following the Commission's winter forecast. Additionally, according to ECB data, in January Spanish monetary financial institutions purchased only EUR 5.3bn in government bonds, well below the EUR 18bn in long-term bonds sold by the Spanish Treasury in the same month, suggesting a very active participation of foreign investors and real money fund in those Treasury issuances.

- **Central Banks will remain supportive**

- Fed chairman Ben Bernanke eased fears of a QE early exit. In his semi-annual testimony before Congress and Senate, Bernanke affirmed that inflation expectations remain well-anchored and that there are no signs of financial destabilization. He noted, "we do not see the potential costs of the increased risk-taking in some financial markets as outweighing the benefits of promoting a stronger economic recovery and more-rapid job creation," suggesting that current Fed policy will last until mid-2013.
- We expect the ECB to let both the monetary policy and the non-standard measures remain unchanged at next week's monetary policy meeting. The main focus will be in the press conference after the meeting, where questions regarding the OMT implementation will garner most of the attention, as the recent political turmoil in Italy prompted a risk in European sovereign debt market. On the other hand, recent euro depreciation comes as a relief to the ECB policy. On liquidity, as the repayments for the second LTRO fell significantly when compared with the first one, the liquidity surplus in the Eurozone remains at a comfortable level (EUR 403 bn). The ECB will not undertake any exit strategy as long as they see signs of significant fragmentation. We do not expect significant changes regarding the ECB's staff macroeconomic projections.
- Following the latest BoE's minutes, where a growing number of members prefer to increase by £25bn the size of the QE, this week BoE's Tucker raised the possibility of imposing negative interest in banks' reserves. The potential increase of QE and the downgrade of Moody's lowered Britain's top AAA credit rating to AA1, are weighing down the pound. Meanwhile, 10Y UK gilt yield decreased by 17 bps despite the downgrade.
- In Japan, Mr. Kuroda was nominated as the next BoJ governor. He will likely pave the way for further monetary easing.
- In Latin America, the central bank of Colombia cut rates, as expected, due to sluggish activity data and positive inflation surprises, but with no signs of further cuts in the near future. Meanwhile, in Peru, the central bank once again increased its reserve requirements to try to moderate the impact of capital inflows on both credit growth and the exchange rate. Next week, Banxico will hold its monetary policy meeting. In Mexico, inflation is expected to increase toward April and then to fall in the last quarter of 2013. This factor, combined with the (dovish) tone of Banxico's statement, suggests that there will be a cut in policy rates of 50 bp in April, once there is more information about the performance of the economy and the inflation

- **The economic recovery very gradual and still fragile**

- In the US, consumer confidence index, ISM manufacturing index and weekly jobless claims, which dropped to its lowest level since June 2008, was better than expected. Regarding the housing market, January purchases of new U.S. homes surged more than expected to a level not seen since July 2008, and pending sales of existing homes rose to their highest level in more than two year and half. In addition, new orders for durable goods excluding transportation climbed more than forecasted in January. Real GDP growth for the 4Q12 grew by 0.1% in a QoQ seasonally-adjusted annualized basis, up from the advance estimate of -0.1% but below consensus expectations.
- The European macro calendar unveiled mixed data. February's economic confidence and final manufacturing PMI index surprised slightly on the upside, but the unemployment rate increased by more than expected. In Germany, economic figures have been quite positive: the GfK leading indicator predicts that consumer confidence will rise in March for a second month in a row, unemployment unexpectedly fell in February and, notably, retail sales surprised on the upside. In contrast, economic data

from Italy were worse than expected, possibly affected by political uncertainty, with the unemployment rate increasing by 0.5 pp in January while the manufacturing PMI decreasing by 2 points in February.

- In Asia, early in the week, both China's February HSBC flash manufacturing PMI and official PMI were worse than expected. However, the outturn was heavily distorted by this year's timing of the Chinese New Year.

Next week: Investors attention will focus on developments with regard to the US 'sequester' measures, the ongoing political negotiation in Italy and the Eurogroup and ECOFIN meetings. On monetary policy, the ECB will hold its monthly meeting. On the economic data agenda, the US February's Payroll figures and the Beige book will be published. Next week will continue to be a busy week for European Treasuries, with Spain, Germany, France and Belgium issuing long-term debt.

Week February, 25 - March, 1

CC	Indicator	Period	Cons. E	Prior	Obs. *
United States	New home Sales (th)	Jan	380.00	378.00	437.00
	S&P/CS Composite 20 (YoY)	Dec	6.62%	5.44%	5.52%
	Consumer confidence	Feb	62.00	58.60	69.60
	Durable good orders ext Transp	Jan	0.2%	1.0%	1.9%
	GDP (QoQ annualize)	4Q12	0.5%	-0.1%	0.1%
	Personal income (MoM)	Jan	-2.4%	2.6%	-3.6%
	Personal spending (MoM)	Jan	0.2%	0.2%	0.2%
	ISM manufacturing index	Feb	52.50	53.10	54.20
	Chicago PMI	Feb	54	55.6	56.8
Euro zone	Economic Confidence	Feb	89.90	89.50	91.10
	Consumer Confidence	Feb F	- 23.6	- 23.6	- 23.6
	M3 s.a. (YoY)	Jan	3.2%	3.3%	3.5%
	Euro-Zone CPI (YoY)	Jan	2.0%	2.0%	2.0%
	PMI Manufacturing	Feb F	47.8	47.8	47.9
	Euro-Zone CPI Estimate (YoY)	Feb	2%	2%	1.8%
	Euro-Zone Unemployment Rate	Jan	11.8%	11.7%	11.9%
Germany	GfK Consumer Confidence Survey	Mar	5.9	5.8	5.9
	Unemployment (K)	Feb	0.0	-14.0	-3.0
	CPI - EU Harmonised (YoY)	Feb P	1.7%	1.90%	1.8%
	Retail Sales (YoY)	Jan	-1.7%	-3.70%	2.4%
	PMI Manufacturing	Feb F	50.1	50.10	50.30
Spain	GDP (QoQ)	4Q12f	-0.7%	-0.7%	-0.8%
	CPI (EU har) (YoY)	Jan	2.7%	2.7%	2.7%
	Current account (bn€)	Jan		1.8	4.9
Japan	Industrial Production	Jan p	-4.8%	-7.9%	-5.1%
	Jobless Rate	Jan	4.2%	4.3%	4.2%
China	HSBC Manufacturing PMI	Feb	52.2	52.3	50.4
	Manufacturing PMI	Feb	50.5	50.4	50.1
Brazil	Unemployment rate	Jan	5.3%	4.6%	5.4%
	GDP (QoQ)	4Q12	0.8%	0.4%	0.6%
Chile	Unemployment rate	Jan	6.2%	6.1%	6.0%

* Forecast: Orange- Below consensus forecast. Green-Above consensus forecast.
Source: Bloomberg and BBVA Research

Calendar: Indicators

Eurozone: Retail sales (January, March 5th)

Forecast: 0.2% m/m	Consensus: 0.2% m/m	Previous: -0.9% m/m
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Retail sales are expected to have increased slightly in January, after the sharp decline of late 2012. This projection implies that the level of sales could remain lower than in the previous quarter, but it also signals clearly a slower pace of deterioration. Consumers' confidence for February improved again mildly, after the marked rise observed in the previous month, pointing to a moderate upward trend in consumers' mood. Nonetheless, recent events in the eurozone, such as the result of Italian elections and the increase of uncertainty surrounding the European debt crisis suggest that sentiment could remain subdued in coming months. Overall, this is consistent with our economic outlook that envisages a more resilient private consumption in early 2013, after the sharp drop expected for 4Q12. Across countries, we think that the divergent trend in households' spending will linger in coming quarters, falling sharply in the periphery and mildly supporting economic growth in core countries, especially in Germany.

Germany: Industrial production (January, March 8th)

Forecast: 0.2% m/m	Consensus: 0.5% m/m	Previous: 0.3% m/m
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We expect industrial production to have increased slightly in January for the second month in a row at a similar rate to that observed in December. In addition, confidence surveys showed a marked improvement in industrial confidence at the beginning of the year, boosted by better expectations about foreign demand. This is in line with our view that the sharp activity fall observed in late 2012 was driven by a sudden stop in exports that is likely to be proved temporary, as activity in emerging economies is gaining momentum at the beginning of the year. Overall, these figures imply that industrial output could increase again over 1Q13 at a similar pace to that observed by-mid 2012 when activity grew at around 0.3% q/q.

US: International Trade Balance (January, March 7th)

Forecast: -\$41.0B	Consensus: -\$43.0B	Previous: -\$38.5B
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Following the significant improvement in the U.S. trade deficit in December, a reversal is likely to take place in January as the latest data point to a slowdown in manufacturing and production export activity. A large driver in the December report was the export of fuels, specifically oil and natural gas. While U.S. production of oil and natural gas continues to rise, we expect that exports of fuels will emerge a bit weaker in January due to political headwinds and still sluggish growth abroad. However, the ISM manufacturing and services reports for January noted continued growth in export orders at a slightly faster pace than imports. Overall, we expect imports to remain relatively subdued due to the weaker dollar in January and ongoing demand for domestic goods such as vehicles and small equipment. With little pent up demand from the holiday season, a weaker import figure and ailing export demand will likely lead to a widening of the trade balance, albeit only for the short term, as trade begins to reignite global demand.

US: Nonfarm Payrolls and Unemployment Rate (February, March 8th)

Forecast: 152K, 7.9%	Consensus: 150K, 7.9%	Previous: 157K, 7.9%
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Nonfarm payrolls are expected to rise in February at a similar pace as in January as economic indicators suggest little disruption in the workforce. February initial jobless claims show some increases in the number of those filing for unemployment benefits, though the monthly average thus far is pretty much on par with January. Consumer confidence reports suggest little change in individuals' outlook on job availability, though overall sentiments have improved since December. The Dallas, New York, Richmond and Philadelphia branches of the Federal Reserve have reported improving employment conditions for February at varying degrees in the manufacturing sector. While the 6-month outlook remains relatively strong, February continues to show little substantive evidence for a decline in the unemployment rate below the 7.8% reached late in 2012. The Federal Reserve has hinted that 2013 is poised to be a strong year for employment but most Fed representatives believe that growth will accelerate later in the year as budgetary issues subside.

China: exports (February, March 8th)

Forecast: 14.5% y/y	Consensus: n.a.	Previous: 14.5% y/y
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Year-over-year export growth is expected to fall sharply in February due to distortions from the timing of the Chinese New Year, which resulted in fewer working days for the month of February compared to last year (and vice versa for January). Given the distortions, a more meaningful gauge of export growth will be the average for January and February combined, which we expect to reach 20.0% y/y, on improving external demand from the US and other Asian economies (especially ASEAN), and also favorable base effects. An outturn in line with our forecast would point to an improving external environment and could boost confidence in the outlook for China's continued growth momentum. Nevertheless, Europe and Japan are likely to remain drags on the export environment in the coming months, and we remain cautious about the overall growth outlook for 2013, with a forecast of 8%. We expect total export growth of 10% (in US dollar terms), up from 8% in 2012.

Markets Data

			Close	Weekly change	Monthly change	Annual change
Interest rates (changes in bps)	US	3-month Libor rate	0.28	0	-1	-19
		2-yr yield	0.23	-1	-3	-4
		10-yr yield	1.85	-11	-14	-12
	EMU	3-month Euribor rate	0.21	-1	-2	-74
		2-yr yield	0.03	-10	-26	-13
		10-yr yield	1.41	-16	-30	-39
Exchange rates (changes in %)	Europe	Dollar-Euro	1.298	-1.6	-4.3	-1.6
		Pound-Euro	0.86	-0.7	0.6	3.7
		Swiss Franc-Euro	1.23	0.1	-0.7	1.7
	America	Argentina (peso-dollar)	5.05	0.3	1.4	16.4
		Brazil (real-dollar)	1.98	0.5	-0.3	14.6
		Colombia (peso-dollar)	1816	1.0	2.2	2.4
		Chile (peso-dollar)	474	0.1	0.6	-2.0
		Mexico (peso-dollar)	12.81	0.8	0.7	0.4
		Peru (Nuevo sol-dollar)	2.60	0.7	1.2	-2.9
	Asia	Japan (Yen-Dollar)	93.28	-0.1	2.4	14.0
		Korea (KRW-Dollar)	1084.56	0.0	-0.1	-2.8
		Australia (AUD-Dollar)	1.021	-1.1	-2.0	-4.9
Comm. (chg %)		Brent oil (\$/b)	110.3	-3.3	-4.0	-10.8
		Gold (\$/ounce)	1575.6	-0.4	-6.1	-8.0
		Base metals	536.9	0.6	-1.3	-1.8
Stock markets (changes in %)	Euro	Ibex 35	8181	0.0	-4.6	-4.5
		EuroStoxx 50	2616	-0.5	-4.2	2.8
	America	USA (S&P 500)	1514	-0.1	0.8	10.5
		Argentina (Merval)	3030	-3.5	-12.5	9.9
		Brazil (Bovespa)	56624	-0.1	-4.6	-16.5
		Colombia (IGBC)	14771	-0.6	-1.5	-2.9
		Chile (IGPA)	22206	0.2	0.4	2.7
		Mexico (CPI)	43861	0.0	-4.1	14.4
		Peru (General Lima)	20603	-0.2	-3.3	-11.1
		Venezuela (IBC)	620809	0.3	25.5	300.9
	Asia	Nikkei225	11606	1.9	4.4	18.7
		HSI	22880	0.4	-4.0	6.1
Credit (changes in bps)	Ind.	Itraxx Main	116	3	5	-15
		Itraxx Xover	447	6	8	-126
	Sovereign risk	CDS Germany	40	-2	-2	-38
		CDS Portugal	392	8	9	-800
		CDS Spain	270	9	7	-102
		CDS USA	42	0	0	---
		CDS Emerging	245	11	16	8
		CDS Argentina	2755	421	745	1968
		CDS Brazil	133	6	19	1
		CDS Colombia	99	-1	2	-22
		CDS Chile	69	-1	-1	-25
		CDS Mexico	103	2	6	-26
		CDS Peru	99	1	3	-38

Source: Bloomberg and Datastream

Weekly Publications

Country	Date	Description
EMU	02/28/2013	➤ Europe Flash - Eurozone - Core inflation slowed in January Core inflation slowed in January
	02/28/2013	➤ Unión Bancaria y el futuro del sistema financiero europeo La fragmentación financiera es incompatible con la UEM. La unión bancaria es una cuestión de supervivencia
	02/27/2013	➤ Flash: "Economic sentiment in the eurozone improves for the fourth month in a row" Economic sentiment in the eurozone improves for the fourth month in a row. Results contrast with falling PMIs in February
Spain	02/28/2013	➤ Financial Systems Flash: Domestic household and business deposits fell by €2 billion and promissory notes by €10 billion in January Domestic household and business deposits fell by €2 billion and promissory notes by €10 billion in January (Spanish version)
	02/28/2013	➤ Flash: Balanza de pagos de diciembre 2012 El déficit de la balanza por cuenta corriente cierra el año 2012 en el -0,8% del PIB.
	02/28/2013	➤ Flash: Contabilidad Nacional Trimestral del 4T12 Tal como se adelantaba en el último número de la revista Situación España, la economía española permaneció en recesión durante el 4T12
	02/28/2013	➤ Flash España: Avance del cierre de la ejecución presupuestaria 2012 El dato de déficit público presentado hoy (un 6,7% del PIB) supone una muy buena noticia
	02/28/2013	➤ Flash España: "Avance del IPC de febrero" El indicador adelantado del IPC de febrero confirma la estabilidad del crecimiento de los precios al consumo
	02/27/2013	➤ Flash España: "Confianza industrial y del consumidor en febrero" En balance, la evolución de las expectativas de los agentes en febrero debe ser valorada positivamente
	02/27/2013	➤ U.S. Flash. Fall in Durable Goods Orders Doesn't Tell the Whole Story New orders for durable goods fell 5.1% but mostly due to transportation. Defense aircraft orders plummeted 63.8% after a 58.5% gain in December
US	02/28/2013	➤ U.S. GDP Flash. Government Spending Cuts Outdone By Better Trade Real GDP growth for 4Q12 revised to 0.1% from an advance estimate of -0.1%. Government consumption and private inventory investment revised down
	02/27/2013	➤ U.S. Flash. Fall in Durable Goods Orders Doesn't Tell the Whole Story New orders for durable goods fell 5.1% but mostly due to transportation. Defense aircraft orders plummeted 63.8% after a 58.5% gain in December
	02/26/2013	➤ U.S. Housing Flash. New Home Sales Surge In January, Prices And Supply Tumble Sales of new homes in January emerged much stronger, up 15.6% to an annual 437K. The ailing supply of homes continues to constrain sales, falling to 4.1 months
	02/25/2013	➤ U.S. Weekly Flash. Headline inflation remains flat but core levels emerge stronger The headline consumer price index (CPI) emerged relatively flat as energy prices continued to fall, somewhat surprisingly given the month's jump in crude oil prices (Spanish version)
Latam	03/01/2013	➤ Latam Daily Flash: "Supportive activity and labor data in Chile and Colombia; Mexico's Energy Plan was released"
	02/28/2013	➤ Latam Daily Flash: "In Peru, reserve requirements were adjusted; survey shows inflation of 0.3%MoM in February in Chile"
	02/27/2013	➤ Latam Daily Flash: "Credit markets moderate in Peru and continue to provide only partial support to activity in Brazil"
	02/26/2013	➤ LatAm Daily Flash - Capital inflows continue to provide funding to current account deficits in Mexico and Peru
	02/25/2013	➤ Latam Daily Flash "Higher than expected inflation in Brazil in Mexico"

Chile

- 02/28/2013 ➤ **Actividad industrial recupera dinamismo y desempleo llega a 6%**
Actividad industrial recupera dinamismo y tasa de desempleo llega a 6% en enero. Con esto, proyectamos un crecimiento del índice de actividad mensual (Imacec) de 6,4% a/a para igual mes.

Peru

- 02/28/2013 ➤ **Peru Economic Outlook. First Quarter 2013**
In Peru, growth forecasts have been revised upwards. GDP is expected to grow by 6.5% in 2013 and 6.3% in 2014.

Mexico

- 02/28/2013 ➤ **Mexico Economic Outlook First Quarter 2013**
Mexico will continue to grow at above 3.0% in 2013

Asia

- 03/01/2013 ➤ **Asia Daily Flash | 1 March 2013: India GDP slows sharply; China PMI falls, remains in expansion; Korea exports contract**
Asian shares were mixed as investors eyed risks from the US spending cuts due to take effect. The Shanghai Composite and Hang Seng slid by -0.3% and -0.6% following the decline in China's PMI data
- 03/01/2013 ➤ **India Flash: Q4 GDP slows sharply on limited fiscal support, leaves room for policy easing in March**
India's real GDP growth slowed sharply in 4Q to 4.5% from 5.3% in Q3 and its lowest growth since March 2009, as decelerating services growth and weak agriculture offset a pickup in industrial activity
- 02/28/2013 ➤ **Asia Daily Flash | 28 February 2013: India delivers Union Budget; Japan IP remains subdued; Korea IP picks up; HK revises land supply policies**
Most Asian markets rose on spillovers from recent positive US economic data and Shinzo Abe's nomination of Haruhiko Kuroda, president of the Asian Development bank, for Japan's central bank governor.
- 02/28/2013 ➤ **India Flash: FY14 Union Budget - credible and pragmatic**
India's budget for FY14: it delivered a credible fiscal consolidation path; it focused on the quality of deficit reduction; it balanced austerity with populism without undermining economic growth. (Chinese version)
- 02/27/2013 ➤ **Asia Daily Flash | 27 February 2013: Hong Kong announces pickup in Q4 GDP, releases annual budget; Japan retail sales remain weak**
Asian equities regained momentum after Bernanke's remarks and better-than-expected US data on consumer confidence and home sales. Japan's Nikkei, however, fell by -1.3% on the yen's strength (+0.3%)
- 02/26/2013 ➤ **Asia Daily Flash | 26 February 2013: HK budget to be announced tomorrow; strong export orders in Taiwan; Singapore IP posts surprise contraction**
Renewed signs of political stability in Italy following inconclusive elections served as a reminder of the external risks still facing Asia. Today Japan's Nikkei fell 2.3% while Hang Seng dropped 1.4%
- 02/25/2013 ➤ **Asia Daily Flash | 25 February 2013: Decisions close on Asian central bank chiefs; China Flash PMI lower; Korea inaugurates eleventh President**
In Japan reports have all but confirmed that Asian Development Bank President will be nominated as the next BoJ chief. The news pushed the yen back to around 94/USD and the Nikkei up by 2.4%

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