

# Global Weekly Flash

## World leaders are concerned about European crisis spillover effects

- **Financial markets' strains eased somewhat early this week on hopes of forthcoming actions to curtail contagion. Yet, volatility in Spanish financial market remains high as investors wait for the publication of the Spanish banking IMF assessment due in coming days and the stress tests from private auditors due in June 21.**
  - The spillover effect of the European debt crisis worried world leaders, who agreed to monitor the crisis closely ahead of the next G20 meeting due on June 18 and 19, thus increasing expectations about a possible coordinate response to the crisis.
  - To reduce the pressure over Europe, the German chancellor said the country is ready to back the use of all existing euro-area instruments in order to stabilize the eurozone. Furthermore, at the next EU Council meeting (28-29 June), European governments might discuss a roadmap toward fiscal and financial union but most of these initiatives seem to be only medium-term goals. Yet, it is very critical to the eurozone to provide a specific timetable for issues such as growth initiatives in countries under problem, a common EZ's banking supervisors, the harmonization of deposit insurance or even the launching of Eurobonds.
  - The sovereign debt auction in Spain faced high demand but pressures on the country are mounting. Following previous S&P action, Fitch has downgraded the Spanish sovereign rating by three notches, from A to BBB, with outlook negative, one notch below S&P and two below Moody's. Fitch sees Spain staying in recession through the remainder of this year and during 2013 as well, while predicts government debt peaking at 95% 2015, assuming a EUR 60bn bank recapitalization. In the short-term, concerns about how the Spanish crisis will be managed are increasing.
  - Further developments in Europe will be closely watched. Next Monday it is expected that the IMF will deliver its forecast for Spanish banks' recapitalization needs, while the two independent analyses will be finalised by June 21st at the latest, according to the Spanish Treasury. Likewise, the Greek election on June 17, the Eurogroup meeting on June 20 or the G20 summit will be key events. In Greece, latest polls showed increasing support for Greece to remain in the euro and for political parties that back the adjustment program. However, the margins are tight.
- **Increasing expectation for Central Banks' policy support: PBoC cut rates, the FED had opened the door for more stimulus in case downside risks persist while the ECB extended the 3M LTRO until the end of the year**
  - The Public Bank of China announced a 25bp cut in interest rates this week. The move was in line with our expectations (though has caused some surprise in the markets) of up to two interest rate cuts in the coming quarters, in addition to further RRR cuts in view of the recent weak economic indicators such as falling inflation and the deteriorating global environment. We expect the current measures taken by the government to help ensure a soft landing, although there are indeed downside risks to our previous 8.3% GDP growth projection for 2012. In our baseline scenario, we forecast another 25bps rate cut and 100 bps cuts in the RRR during Q2/Q3.
  - As expected, the ECB kept interest rate unchanged at 1%, though a minority voted for a rate cut. There were no hints on the possibility of further 3Y LTROs and/or the reactivation of the SMP. The ECB (still) wants governments to do more as it sticks to its view that monetary policy alone cannot fix all problems "It is not right for monetary policy to fill in for other's lack of action". However, the ECB will continue supporting liquidity in the banking system through 3M LTRO until the end of the year. Likewise, BoE left its policy rate unchanged.

- Meanwhile, expectations for further policy actions by the FED have tempered after Fed Chairman Ben Bernanke refrained from sending a clear signal on whether he supports or not additional actions to spur growth. However, early in the week, three FED members suggested the FED should be prepared to take actions if the economy deteriorates further. The FED Atlanta President Dennis Lockhart said extending Operation Twist is an “option on the table” and that “there is capacity to do more”. The next FOMC meeting will take place on June 19-20.

- **Recent economic data showed that the world economic activity is suffering from the spillover effect of the European debt crisis**

- In the EZ, 1Q12 stagnation was confirmed. The economy escaped from falling back into recession in the 1Q12 after contracting 0.3% q/q in the 4Q11. We now expect economic activity to weaken in the 2Q12 (MICA-BBVA: -0.2% q/q). Private sector activity seems to have fallen deeper in contraction during May. Final EZ PMI-Composite (46.0) was in line with flash figures and worse than April's (46.7), with the Services sub-index remaining almost unchanged at 46.7 (Flash 46.5, April 46.9). Country divergences narrowed, as output fell across the four largest economies. Besides, Germany exports dropped by 1.7% m/m, while imports fell by 4.8%. These figures suggest that Germany is feeling the effect of the eurozone slowdown.
- Mixed economic data from the US haven't lifted concerns. The moderation in the employment trend and the recent fall in equity indexes might weigh on US confidence indicators in the coming month. The ISM-Services gained a little in May to 53.7, while Factory orders in April surprised to the downside, dropping further.
- The decrease in Asian trade figures reinforced growth concerns in the area, as European crisis' spillover weigh on the global trade. Taiwan reported declines in both exports and imports in May while Malaysian exports declined again in April, by -0.1% y/y (consensus: +1.6% y/y), the second consecutive drop on a y/y basis, as exports to the US and Japan dropped by -1.7% y/y and -3.4% y/y respectively.
- Inflation in Latin-American was slightly above our expectation in Mexico and Colombia. The Mexican CPI spiked from 3.4% in April to 3.9% in May. In our view, Inflation will close the year below 4%. In Colombia, annual inflation is at 3.4%. We expect inflation to remain relatively stable, waiting for a further slowdown in food prices' inflation and for moderate pressures on the demand side (though we estimate a positive output gap over the next quarters). Elsewhere, in Brazil inflation dropped to 4.99% y/y in May from 5.11% in April. Inflation has been declining uninterruptedly since September 2011. We expect this downward trend to end in June, leaving the Central Bank in a less comfortable situation to continue cutting interest rates.

**Next week:** Next Monday it is expected the IMF to deliver its forecast for Spanish banks' recapitalization needs. In France, legislative elections will take place on June 10. Over this weekend, China will release the industrial production, inflation and trade figures for May, which could set the tone for next week's market moves. In the US, June's Consumer Confidence and May's Retail Sales and Industrial Production will be published.

# Calendar: Indicators

## Eurozone: Industrial production (April, June 13th)

Forecast: -1.1% m/m

Consensus: -1.0% m/m

Previous: -0.3% m/m

Industrial output is expected to have declined significantly in April, after falling slightly in March, in line with some national figures already released (Germany and Spain). Manufacturing confidence, both from PMI and the European Commission, also showed gloomy prospects for the industrial sector in April and May, with the former remaining clearly in contractionary territory and the latter below its long-term average. Overall, April's forecast implies that industrial output could have declined by around -1% over the first quarter, but also that the deterioration should not be as deeper as that registered in the last quarter of 2011 (-2.0% q/q). Given the high correlation between the industrial sector and the economic cycle, all these figures point to another GDP fall in the current quarter. In particular, our MICA model estimates a GDP decline of around -0.2% q/q in Q2 12.

## Eurozone: HICP inflation (May, June 14th)

Forecast: 2.4% y/y

Consensus: 2.4% y/y

Previous: 2.6% y/y

We expect headline inflation to be confirmed at 2.4% y/y in May, easing by 0.2pp from April. Taking into account recent fuel prices, our forecasts had also projected this deceleration, instead of a -0.1pp previously estimated. Therefore, May's price developments stemmed from lower inflation in more volatile components, especially energy. In contrast, inflation of the rest of the components is expected to have remained broadly stable, resulting in unchanged core inflation at 1.9% y/y. Looking forward, we expect a slower moderation of inflation in coming months, remaining above the ECB target during 2012, although returning to the target by the end of the year. Core inflation is likely to remain hovering around 1.9% y/y in coming months to moderate timidly in the second half of the year.

## US: Retail Sales, Ex Auto (May, June 13th)

Forecast: -0.1% m/m, 0.0% m/m

Consensus: 0.0% m/m, 0.0% m/m

Previous: 0.1% m/m, 0.1% m/m

Retail sales decelerated significantly in April and are expected to slow once again in May. Auto sales for the month dropped 4.0% to the lowest annual rate of the year, while falling gasoline prices should again weigh on the headline figure. While easing at gas pumps may have encouraged increased discretionary spending for May, consumer confidence reports were mixed. Weekly retail reports have dropped significantly from April, with chain store sales data suggesting minimal improvement for the core figure. In general, we expect that European worries and weakening employment conditions limited consumer willingness to spend in May.

## Consumer Price Index, Core (May, June 14th)

Forecast: 0.2% m/m, 0.2% m/m

Consensus: -0.2% m/m, 0.2% m/m

Previous: 0.0% m/m, 0.2% m/m

Consumer price inflation is expected to ease again in May on account of further declines in energy prices. In particular, crude oil prices have dropped significantly from April's levels, while other commodity price indices have fallen less dramatically. Weakening consumer activity may limit upward pressure on core prices, and overall consumer inflation expectations are down for one and five-years ahead. Still, food, medical care, and shelter prices continue to increase at a steady pace.

## China: New Yuan loans (May; June 11-15th)

Forecast: 680 bn RMB

Consensus: 705 bn RMB

Previous: 682 bn RMB

Credit growth will be closely watched following the release of May activity and inflation indicators on June 9-10. Concerns about sluggish credit growth and slowing activity have prompted an increasingly proactive policy response by the authorities, including recent cuts in the RRR and a just-announced interest rate cut effective June 8. The latter is intended to boost the demand for credit. In this regard, the May credit outturn will help guide market expectations on the extent of further policy easing. We expect new loans for May to be broadly similar to the previous month, based on lending indicators of the 4 largest banks. Cumulative new loans through April amounted to RMB 3.14 trillion, compared to an informal full-year target of RMB 8.5 trillion (loan growth is behind target given that new loans are usually higher toward the beginning of the year).

# Markets Data

			Close	Weekly change	Monthly change	Annual change
Interest rates (changes in bps)	US	3-month Libor rate	0.47	0	0	22
		2-yr yield	0.27	2	1	-13
		10-yr yield	1.58	13	-24	-139
	EMU	3-month Euribor rate	0.66	0	-3	-81
		2-yr yield	0.06	5	-1	-148
		10-yr yield	1.32	15	-20	-164
Exchange rates (changes in %)	Europe	Dollar-Euro	1.247	0.3	-3.5	-13.1
		Pound-Euro	0.81	-0.1	0.8	-8.6
		Swiss Franc-Euro	1.20	0.0	0.0	-0.7
	America	Argentina (peso-dollar)	4.48	0.3	1.0	9.5
		Brazil (real-dollar)	2.03	-0.4	3.2	27.3
		Colombia (peso-dollar)	1770	-3.3	0.1	-0.4
		Chile (peso-dollar)	500	-3.5	2.5	7.0
		Mexico (peso-dollar)	14.17	-1.0	4.9	19.0
		Peru (Nuevo sol-dollar)	2.68	-1.0	1.2	-3.0
	Asia	Japan (Yen-Dollar)	79.24	1.6	-0.5	-1.3
		Korea (KRW-Dollar)	1175.30	-0.2	3.1	8.6
		Australia (AUD-Dollar)	0.983	1.3	-2.2	-6.7
Comm. (chg %)		Brent oil (\$/b)	97.6	-0.9	-13.8	-17.9
		Gold (\$/ounce)	1569.8	-3.3	-1.2	2.5
		Base metals	511.4	0.3	-4.5	-15.7
Stock markets (changes in %)	Euro	Ibex 35	6332	4.4	-7.1	-36.4
		EuroStoxx 50	2111	2.1	-5.1	-22.7
	America	USA (S&P 500)	1315	2.9	-2.9	3.5
		Argentina (Merval)	2228	0.6	-4.6	-31.0
		Brazil (Bovespa)	54156	1.4	-9.4	-13.6
		Colombia (IGBC)	14149	0.1	-6.7	-1.8
		Chile (IGPA)	20641	0.0	-4.4	-8.1
		Mexico (CPI)	37247	0.2	-4.8	6.5
		Peru (General Lima)	21020	1.5	-2.5	1.7
		Venezuela (IBC)	240345	-1.0	-10.2	196.5
	Asia	Nikkei225	8459	0.2	-6.5	-11.1
		HSI	18502	-0.3	-9.0	-17.5
Credit (changes in bps)	Ind.	Itraxx Main	174	-10	18	66
		Itraxx Xover	699	-39	5	299
		CDS Germany	105	3	16	65
	Sovereign risk	CDS Portugal	1112	-73	5	373
		CDS Spain	572	-31	56	299
		CDS USA	49	0	8	---
		CDS Emerging	308	-14	46	86
		CDS Argentina	1394	-100	406	798
		CDS Brazil	163	-12	31	51
		CDS Colombia	152	-13	32	46
		CDS Chile	121	-13	22	49
		CDS Mexico	152	-17	31	45
		CDS Peru	165	-11	32	21

Source: Bloomberg and Datastream

# Weekly Publications

Country	Date	Description
USA	07/06/2012	<p>&gt; <b>U.S. Banking Watch. Consumer Credit: Monthly Situation Report</b> Seasonally-adjusted consumer credit increased \$6.5bn in April, a significantly slower pace compared to the previous few months. Nonrevolving credit growth accelerated slightly to \$10bn</p>
	07/06/2012	<p>&gt; <b>U.S. Banking Watch. FDIC Banking Profile 2012Q1</b> Bank Earnings Climb as Asset Quality Rallies</p>
	05/06/2012	<p>&gt; <b>Canada Flash. BoC maintains that "some withdrawal" of monetary stimulus may be necessary, but reaffirms downside risks</b> In today's interest rate decision, the BoC reaffirmed their position that "some modest withdrawal of the present considerable monetary policy stimulus" may be needed</p>
	04/06/2012	<p>&gt; <b>U.S. Weekly Flash. Nonfarm payrolls rose 69K while the unemployment rate increased to 8.2% in May</b> Today's BLS report reflects worse-than-expected employment situation and increased uncertainty about the economic recovery in the coming months (<i>Spanish version</i>)</p>
EMU	06/06/2012	<p>&gt; <b>ECB Watch: "It would not be right for the ECB 'to fill for other institutions' lack of action"</b> As expected, the ECB left the key policy rate unchanged at 1.0% at today's monetary policy meeting. The decision was taken by very broad consensus (<i>Spanish version</i>)</p>
	06/06/2012	<p>&gt; <b>Artículos de Prensa: El euro: hacia una solución cooperativa y dinámicamente consistente</b> El éxito del BCE en el anclaje de las expectativas de inflación en la Eurozona se ha basado en una solución de manual</p>
	06/06/2012	<p>&gt; <b>Europe Flash: "Stagnation in Q1 confirmed by second GDP estimate"</b> Unrevised, flat GDP growth during Q1, with persistent country divergences. External demand once again the driver of growth</p>
Spain	06/06/2012	<p>&gt; <b>Flash España: "Producción industrial en abril"</b> De cara a los próximos meses, los indicadores adelantados de la actividad en el sector no anticipan una mejora</p>
	04/06/2012	<p>&gt; <b>Flash España: "Afiliación a la Seguridad Social y desempleo registrado en mayo"</b> Pese a que mayo es un mes estacionalmente positivo, los registros del mercado laboral confirman que el deterioro de la actividad continuará en el segundo trimestre del año.</p>
Latin America		
Brazil	06/06/2012	<p>&gt; <b>Brazil Flash: "Inflation continued to fall in May, but downward trend is expected to end soon"</b> Inflation continued to fall in May, but downward trend is expected to end soon.</p>
Chile	05/06/2012	<p>&gt; <b>Flash Chile: En línea con lo esperado, actividad económica creció 4,8% a/a en abril</b> El Índice Mensual de Actividad Económica (IMACEC) creció 4,8% a/a, con un incremento de 0,5% m/m en la serie desestacionalizada, en línea con las expectativas.</p>
	04/06/2012	<p>&gt; <b>Flash Chile: Banco Central discutió opciones de mantención y alza en su reunión de mayo ¿Hará lo mismo en junio?</b> El Índice Mensual de Actividad Económica (IMACEC) creció 4,8% a/a, con un incremento de 0,5% m/m en la serie desestacionalizada, en línea con las expectativas.</p>
Colombia	05/06/2012	<p>&gt; <b>Flash Colombia. Inflación mantuvo resultado favorable en mayo</b> La variación mensual del IPC se ubicó en 0,30%, ligeramente por encima de lo esperado (BBVA: 0,25% m/m; consenso: 0,21% m/m), llevando la inflación anual a 3,44%</p>
Peru	07/06/2012	<p>&gt; <b>Flash Peru: Política monetaria: sin cambios en tasa pero con una mayor atención en los riesgos externos</b> En línea con lo que el mercado esperaba, el Banco Central mantuvo en junio la tasa de interés de referencia en 4,25%.</p>
	04/06/2012	<p>&gt; <b>Flash Peru: Cuentas nacionales al primer trimestre confirman poco impacto de la turbulencia internacional</b> En el primer trimestre, la actividad económica se aceleró al crecer 6,0% a/a (5,5% en 4T11) debido al mayor impulso de la inversión (privada y pública) y de las exportaciones.</p>

## Mexico

- 07/06/2012 ➤ **Mexico Inflation Flash. May 2012 inflation: the most volatile prices push inflation towards 4%, a spike that will reverse after the summer**  
General: Actual:-0.32% m/m vs. BBVA:-0.26% m/m Consensus:-0.34% m/m. Core: Actual: 0.27% m/m, vs. BBVA:0.25% m/m, Consensus:0.27% m/m (*Spanish version*)
- 06/06/2012 ➤ **Mexico Flash. Banxico: No change in monetary policy rate. Special attention on foreign developments**  
Considering the spike in global risk aversion lower than expected US growth data, a moderate increase in inflation and an exchange rate depreciation do not modify neutral balance of risks for inflation (*Spanish version*)
- 04/06/2012 ➤ **Mexico Real Estate Flash. Twice seven**  
Housing reflects the trend in building, but as a mirror image. Our forecast growth in building went up in smoke, like Canek's sacrifice to the gods (*Spanish version*)

## Asia

- 07/06/2012 ➤ **Asia Daily Flash | 7 June 2012: China cuts interest rates; Taiwan's exports contract in May; Upbeat jobs data in Australia**  
As we send out today's Daily Flash, news has just come of a 25bps interest rate cut in China.
- 07/06/2012 ➤ **China Flash: China cuts interest rates amidst weak economic data, and introduces greater rate flexibility**  
The PBoC announced a 25bp cut in interest rates late today after Asian markets had closed. The move is in line with our expectations of up to two interest rate cuts in the coming quarters.
- 07/06/2012 ➤ **China Flash: China confirms postponement of Basel III implementation**  
The State Council yesterday confirmed a one-year postponement in the start of Basel III implementation to January 2013.
- 06/06/2012 ➤ **Asia Daily Flash | 6 June 2012: Australia's GDP surged in Q1; China announces a new timetable for implementing Basel III**  
A better-than-expected GDP outturn in Australia provided a welcome lift to sentiment, with the region's stock markets up for a second consecutive day (except for China).
- 05/06/2012 ➤ **Asia Daily Flash | 5 June 2012: Australia cuts interest rates; India's central bank deputy governor hints at rate cut**  
In line with expectations, the Reserve Bank of Australia cut its policy rate by 25 bps to 3.50%, citing modest domestic growth and a weak global environment.
- 04/06/2012 ➤ **Asia Daily Flash | 4 June 2012: China issues guidelines for further financial system reform**  
Last Friday's weaker-than-expected US jobs data triggered a selloff in Asian markets today. The Korean and Chinese stock markets were among the biggest decliners.

## Emerging Markets

- 05/06/2012 ➤ **Economic Watch: World trade indicators keep momentum despite global uncertainties**  
Trade momentum remained in positive territory in March consolidating the recovery in exports markets. (*Chinese version*)

## EAGLEs

- 06/06/2012 ➤ **EAGLEs Quarterly Report. Second Quarter 2012**  
Recent activity indicators in most of the EAGLEs show lower than expected marks.
- 05/06/2012 ➤ **EAGLEs Flash: EAGLEs citizens are pushing up the demand for tourism services but they are also increasingly relevant destinations for travellers worldwide**  
In the last six years EAGLEs citizens' expenditure in international tourism services has more than doubled, whereas in the case of the G7's it has barely grown.

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