Global Weekly Flash

Some relief in European sovereign risk premium

- This week's bilateral meetings between top European leaders and the IMF's managing director have brought expectations about soften fiscal consolidation requirements in Europe and the promotion of growth and job creation without breaking fiscal discipline commitments in the EZ. This would be a significantly change in the management of the sovereign crisis, since up to this moment the reduction of the government debt was expected to occur through austerity. Chancellor Merkel has stressed that European Union's Structural Funds could be used more efficiently to promote growth. Nevertheless, it would be quite premature to bet on this direction. The next EU council meeting, at the end of January, could bring some clues of this new approach to deal with the European crisis. Additionally, European authorities are conscious about the need of a quick agreement on the Greek PSI and the second bail-out program. Nevertheless, according to press reports, bondholder participation rate on Greek debt swap is currently below 75%, which means that official sectors should increase their bail-out, and this is not take for granted. The second bail-out program is due to be discussed next week between Greece and "Troika" officials.
- Good demand in this week's European sovereign auctions, as most issuers met or surpassed their debt issuing targets. Spain sold EUR 9.89bn in bonds. The total amount was significantly above the EUR 4-5 target range initially set by the Spanish government, and the yields were below those registered in the secondary market and way smaller than previous auctions. Italy also has succeded in its auctions, as well as Germany and France. Italian and Spanish 10Y spread has narrowed significantly (more than 60bp) over the week.
- Today the bank of Spain released the data of Spanish banks' borrowing from ECB. The data showed total net borrowing was EUR118.9 bn, up from EUR97.97 bn in November, near the highest level achieved in July 2010. Also this week the Italian central bank announced the ECB funding to Italian lenders rose to EUR201 bn in December from EUR153.2bn in November. Borrowing from the ECB in December rose significantly due to the first 3Y auction held last month.

- **ECB and BOE hold interest rates, as expected, but the former let the door open for a rate cut. In Emerging Markets, easing inflation in China paves the way for more policy easing, while in Latam the Chilean Central Bank joints the Brazilian in a preemptive move despite high inflation**
  - As widely expected, the ECB left interest rates on hold at 1.0%. The ECB retained a dovish tone while it signalled that at this stage it is cautiously alert as it assesses the effects of recent policy moves. The ECB thinks that the three-year LTRO was successful in avoiding a "credit crunch", and it anticipates substantial demand at the next three-year LTRO (29 February) as a broader collateral base will likely apply. As the ECB wants to take hold of recent policy moves, a potential additional rate cut would depend on the market effects of the three-year LTROs, the evolution of sovereign tensions, the degree of deterioration in economic activity and the absence of inflation pressures. Having said that, we continue to think that activity will continue on a moderate downward trend, while further easing in financial tensions will be gradual and volatility will remain high. Therefore, our base scenario continues to be a 25bp rate cut on 8 March, but the odds that it would take place further ahead seem to have increased somewhat today.
  - In China lower inflation (CPI 4.1%y/y in December vs 4.25 in November) and weak imports figures in December has paid the way for further monetary policy easing to support growth. We expect additional 150-200bp cuts in the reserve requirement ratio (RRR) in 1H12, whit the next cut likely in the coming month or two. If the external environment deteriorates further, we would also expect up to 50bp cuts in interest rates in the second or third quarter of the year. We support our idea of a soft landing in Chinese Economy. Moreover increasing room to ease monetary policy dispel risk of a hard landing in this economy. Both Indonesia and Korea kept interest rates unchanged, as expected, although cuts are anticipated later in the year.
  - In Latinamerica, upside surprises on recent inflation data (México, Chile and Colombia) could have contributed to reduce expectations on rate cuts. However, Bank of Chile surprised the markets cutting interest rates by 25bps to 5%, dismissing the relevance of December's upward inflation surprise. With this preemptive move, the Central Bank of Chile joints Brazil, while Peru held interest rate at 4.5%.

- **Economic data showed that the US activity continues improving but at a moderate pace while in the EZ there are signs of a mild recession**
  - The Beige book confirmed the slightly improvement seen in real economic data in the US recently. All Fed's district reported expansion but suggesting only a moderated growth. Retail sales increased less than-expected in December but figures for November and October were revised upwards bringing a sound personal consumption growth in the 4Q'11. Even though the improvement seen in the US economic activity in the last quarter of 2011, the uncertainties about European sovereign debt crisis and the impact of the household and the banking sector deleveraging on the US economy will prevent the FED against a change in its monetary policy outlook. The Fed is still focusing on mortgage rates— through yield curve adjustments— and mortgage-backed securities (MBS) markets, in this way they released a brief outlining the economic challenges facing the housing market.
  - In Europe, Germany registered a growth of 3%, with strong domestic demand, while GDP growth in Q4 is expected to have turned negative. At the same time Germany saw its public finances improving, with a small deficit for 2011 (1%). For the eurozone as a whole, we continue to forecast a fall of -0.2/-0.3% q/q at the end of the year, and after today's revision of the Q3 figure, we now expect annual growth in 2011 to be 1.5% instead of 1.6%. Furthermore, industrial production in the eurozone fell by 0.1% m/m in November from a revised fall of 0.3% y/y. This data suggest a weak picture for industrial activity in the eurozone in line with manufacturing PMI released previously.
  - In China December trade figures showed that export growth remained buoyant at 13.4% y/y. But import growth decelerated to 11.8% y/y from 22.1% in November, a possible sign of weakening domestic demand. On the other hand, new loans increased by more than expected, to RMB 640.5 billion, up from RMB 562.2 billion in November.
  - In Brazil retail sales expanded 1.3%m/m in November, significantly more than expected. The figure is line with a GDP growth of around 0.3%q/q in Q4. and reinforces the view that economic activity rebounded in the end of the year after due the announcement of some countercyclical measures. This recovery could reduce the room for the CB to cut interest rates, which is consistent with our call of (only) two additional 50bps cuts of the SELIC (markets are, in general, pricing three or four 50bps cuts this year). In Mexico inflation raised 0.82% mom ending the year at 3.82% y/y below 4% which is the upper bound of Banxico's variability range for its 3% objective. The inflation was driven by its more volatile components. The pressure from rising import costs and energy prices outweighs the lack of demand pressures.

NEXT WEEK: meetings between top European leaders will continue ahead of the ECOFIN meeting on January 23. Chancellor Merkel will meet with President Sarkozy and PM Monti, while Mr Van Rompuy will meet Spanish PM Rajoy. On the economic side, China will release the 4QGDP11 GDP figures along with other activity data. Regarding government debt issuance, next week is less relevant although Spain and Germany will sell bonds and Greece and Portugal will test the market selling Bills.

Calendar: Indicators

Eurozone: HICP inflation (December, January 17th)

Forecast: 2.8% y/y	Consensus: 2.8% y/y	Previous: 3.0% y/y

We expect inflation to slow down in December by 0.2pp due to favourable base effects in energy prices, while core inflation is expected to have remained stable at 1.9% y/y. Looking forward, the moderation in headline inflation should continue at the beginning of 2012, reverting below the ECB target late at the end of the first quarter. Inflationary pressures are expected to ease further in coming months due to the weakness of domestic demand, but several factors have appeared in recent weeks that could put a brake to this deceleration or even trigger higher inflationary pressures again, such as the depreciation of the euro, a minor slowdown in oil prices than anticipated and potential hikes in both taxes and administered prices to meet fiscal targets.

Germany: ZEW economic sentiment (January, January 17th)

Forecast: -52.0	Consensus: -49.8	Previous: -53.8

We expect financial experts' expectations on economic activity for the next six months to have increased slightly in Juanuary for the second month in a row, confirming the interruption of the downward trend observed since the second quarter of 2011. Nevetheless, the ZEW economic sentiment remains clearly below its historical average. In contrast, the indicator of the current situation is expected to have declined further at the beginning of the year, revealing more worriying signs after Destatis advanced that German economy contracted by around -0.2% q/q in Q4. Overall, these figures suggest that the economy could contract again in Q1, but pointing to an improvement over the second half of the year.

US: Industrial Production (December, January 18th)

Forecast: 0.4% m/m	Consensus: 0.5% m/m	Previous: -0.2% m/m

Industrial production dropped in November for the first time since April 2011, dragged down by weakness in the auto sector. According to regional Federal Reserve surveys, the manufacturing sector has rebounded in December and durable goods orders remain strong. Furthermore, manufacturing employment jumped significantly, signaling an increase in activity for the month. In general, production is expected to grow in December to make up for losses in the previous month and will continue to approach pre-recession levels.

US: Consumer Price Index, Core (December, January 19th)

Forecast: 0.1%, 0.1% m/m	Consensus: 0.1%, 0.1% m/m	Previous: 0.0%, 0.2% m/m

Headline inflation has been lower-than-expected in the past two months and will likely increase only slightly in December. The energy component of CPI declined in both October and November and appears to have fallen again in December as suggested by a decline in crude oil prices. Food inflation has been decelerating but is likely to remain positive. Import prices likely increased for the month, while rent prices continue to exert pressure on inflation. Excluding food and energy, core inflation is expected to continue easing due to excess resource slack.

China:GDP (Q4, January 17th)

Forecast: 8.2% y/y	Consensus: 8.7% y/y	Previous: 9.1% y/y

China’s Q4 GDP outturn will be watched for further signs of a growth slowdown. GDP growth slowed in Q3 to 9.1% y/y from 9.5% in Q2. Based on high frequency indicators such as manufacturing PMI, the pace of the slowdown appears to have accelerated in recent months due to weakening external demand. We expect GDP growth to have slowed further in Q4, which would bring full-year growth for 2011 to 9.0%. With inflation continuing to fall, the authorities have recently shifted their policy stance toward supporting growth. A recent easing in the monetary stance and supportive fiscal policy should help sustain domestic demand; we expect growth to bottom out in the first half of 2012. In addition to GDP, a number of important monthly indicators will also be released next week, including industrial production, investment, and retail sales.

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Markets Data

				Close	Weekly change	Monthly change	Annual change
Interest rates	(changes in bps)	US	3-month Libor rate	0.57	-1	1	26
			2-yr yield	0.23	-3	-1	-34
			10-yr yield	1.89	-6	-1	-143
		EMU	3-month Euribor rate	1.23	-6	-19	23
			2-yr yield	0.16	-1	-12	-100
			10-yr yield	1.80	-5	-12	-123
Exchange rates	(changes in %)	Europe	Dollar-Euro	1.278	0.5	-1.6	-4.2
			Pound-Euro	0.83	1.0	-0.8	-0.9
			Swiss Franc-Euro	1.21	-0.5	-2.1	-6.0
		America	Argentina (peso-dollar)	4.31	-0.1	0.7	8.5
			Brazil (real-dollar)	1.78	-4.0	-5.0	5.6
			Colombia (peso-dollar)	1840	-2.1	-5.1	-1.6
			Chile (peso-dollar)	501	-1.7	-3.8	2.4
			Mexico (peso-dollar)	13.55	-1.3	-2.6	12.3
			Peru (Nuevo sol-dollar)	2.69	-0.1	-0.2	-3.4
		Asia	Japan (Yen-Dollar)	76.74	-0.4	-1.7	-7.5
			Korea (KRW-Dollar)	1148.60	-1.0	-0.9	2.9
			Australia (AUD-Dollar)	1.034	1.1	4.2	4.4
Comm.	(chg %)		Brent oil ($/b)	110.6	-2.1	5.4	12.1
			Gold ($/ounce)	1639.6	1.3	4.2	20.4
			Base metals	526.9	1.2	2.4	-10.8
Stock markets	(changes in %)	Euro	Ibex 35	8515	2.7	4.1	-18.0
			EuroStoxx 50	2365	2.9	7.2	-19.0
		América	USA (S&P 500)	1296	1.4	6.9	0.2
			Argentina (Merval)	2820	1.8	17.1	-20.3
			Brazil (Bovespa)	59921	2.3	5.8	-15.5
			Colombia (IGBC)	13080	1.1	5.4	-13.8
			Chile (IGPA)	20318	0.4	2.2	-12.3
			Mexico (CPI)	37321	1.4	3.6	-1.8
			Peru (General Lima)	20540	3.7	6.4	-5.7
			Venezuela (IBC)	117666	1.3	0.5	78.5
		Asia	Nikkei225	8500	1.3	-0.2	-19.0
			HSI	19204	3.3	4.6	-20.9
Credit	(changes in bps)	Ind.	Itraxx Main	171	-6	-20	67
			Itraxx Xover	717	-35	-96	304
		Sovereign risk	CDS Germany	101	-11	-5	41
			CDS Portugal	1063	-52	-61	582
			CDS Spain	394	-56	-53	94
			CDS USA	48	-3	-5	---
			CDS Emerging	303	-11	-14	103
			CDS Argentina	884	2	-77	352
			CDS Brazil	159	-2	-2	53
			CDS Colombia	152	0	-3	44
			CDS Chile	127	-2	-1	48
			CDS Mexico	151	-1	-7	42
			CDS Peru	179	4	5	74

Source: Bloomberg and Datastream

Weekly Publications

Country	Date	Description
Spain	01/10/2012	**Flash España:** “Compraventa de viviendas en noviembre de 2011" El número de compraventas de viviendas durante el mes de noviembre se recupera respecto a los dos meses anteriores y, corrigiendo la serie de variaciones estacionales y efectos de calendario, se observa un crecimiento del 14,3% m/m, el mayor del último año y medio.
	01/09/2012	**Flash España:** “Confianza industrial y del consumidor en diciembre**”** La confianza continuó revelando señales mixtas en diciembre. Así, mientras que la confianza de los consumidores e mantuvo estable -a razón de las movimientos contrapuestos de sus componentes-, se consolidó claramente la tendencia a la baja en el caso de la confianza industrial.
Europe	12/01/2012	**ECB Watch:** “ECB: cautiously alert while it assesses the effects of recent policy moves**”** As widely expected, the ECB left interest rates on hold at 1.0%. The ECB retained a dovish tone while it signalled that at this stage it is cautiously alert as it assesses the effects of recent policy moves. The ECB thinks that the three-year LTRO was successful in avoiding a “credit crunch”, and it anticipates substantial demand at the next three-year LTRO (29 February) as a broader collateral base will likely apply.
	01/11/2012	**Flash Europe:** “Germany. GDP: 3% in 2011, but probable fall in Q4” Germany registered a growth of 3%, with strong domestic demand, while GDP growth in Q4 is expected to have turned negative. At the same time Germany saw its public finances improving, with a small deficit for 2011 (1%). For the Eurozone as a whole, we continue to forecast a fall of -0.2/-0.3% q/q at the end.
US	01/09/2012	**Weekly Flash:** “Employment surprises to the upside, ISM indices point to modest expansion” The employment report for December surprised to the upside with improvements in both nonfarm payrolls and the unemployment rate. *(Chinese version).(Spanish version)*
	01/12/2012	**Fed Watch:** “Federal Reserve Balance Sheet” Balance sheet reflects mortgage objectives of white paper.
	01/12/2012	**US Economic Watch:** “Modest recovery with elevated uncertainties” 2012 GDP growth will remain moderate at 2.3%, a slight improvement from the 1.8% gain in 2011. Inflationary risks are low, amid elevated slack in the economy.
	01/12/2012	**Economic Watch:** “Job Creation in 2012 will not Impress” Improvements in initial claims belie longer-term issues.
	01/02/2012	**Banking Watch:** “Consumer Credit: Monthly Situation Report” Total outstanding consumer credit nearly doubled expectations in November, increasing by \$20.4bn MoM on a seasonally-adjusted basis (BBVA: \$11.0bn).
Latin America		
	01/09/2012	**Weekly Watch:** “Inflation pressures at the end of 2011" Monthly Inflation in December was higher than expected in Chile and Colombia, meanwhile in Peru and Brazil figures were in line with expectations. *(Spanish version)*
Mexico	01/12/2012	**Mexico Flash:** “Bank deposits: Total bank deposits have shown two digit rate of growth from January to November 2011” In November 2011 total bank deposits continued its two digit rate of growth, and in that month its annual nominal growth rate was 12.4%.
	01/10/2012	**Mexico Flash:** “Bank loans to the private sector: continue to grow at high rates and in November accumulate 20 months of continued growth” In Nov. 2011 the annual nominal rate of growth of bank loans granted to the private sector was 15.2%. Greater than the one of the previous month (14.1%) and it was also greater than the one of the same month of 2010 (8.6%).
	01/09/2012	**Mexico Flash:** “Building continues to grow” For the second consecutive month, building activity has increased at a monthly growth rate of at least 10 point.

01/09/2012 **Mexico Flash:** "December 2011 inflation, above market consensus"
The raise in costs outweighs the lack of pressure from domestic demand. CPI: Observed: 0.82% mom vs BBVA: 0.71% mom Consensus: 0.72% mom. Core: Observed:0.51% mom vs BBVA: 0.44% mom Consensus:0.48% mom.

01/13/2012 **Situación Inmobiliaria México Enero 2012:** "El crédito hipotecario, fuerzas encontradas entre oferta y demanda"
- La población no afiliada amplía el potencial del mercado hipotecario, aunque será clave el desarrollo de productos adecuados.
- Los bancos de tierra, modelo que debe aprovecharse mejor Plan Financiero Infonavit, una agenda estratégica con un enfoque hacia el derechohabiente.

Asia

India

01/12/2012 **India Flash:** Industrial production picks up in November
Capital goods sector expected to see a temporary pickup in the run up to important state elections.

China

01/12/2012 **China Flash:** Easing inflation provides policy room to support growth
Headline CPI inflation eased to 4.1% y/y in December from 4.2% in November, in line with expectations (Consensus: 4.0%; BBVA: 4.1%.

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