

Global Weekly Flash

Central bankers prepare ahead of Greek elections on Sunday

Market fears over a (near-term) potential Greek exit intensified this week ahead of Greek elections on Sunday. The main concerns are related to contagion. Facing huge risks, policy makers have undoubtedly strong incentives to compromise, tackle the crisis and avoid a Greek exit. Central bankers prepare ahead of Greek elections: coordinated Central Banks' action is expected if financial markets conditions deteriorate further.

- Greek elections are in the spotlight. Anger seems to have been replaced by the fear of an ungoverned country and an euro exit. The most recent opinion polls clearly suggest that no party would obtain the necessary support to form a government on its own. New Democracy, the center-right conservative party, is on the lead while the left-wing SYRIZA comes in second (by a 1.4-2.5p margin). Only one of the last six opinion polls shows SYRIZA coming first (by 6p). The most probable outcome is drawn with the ND forming a coalition government with PASOK (and maybe a third party). Another scenario is traced with SYRIZA coming first and forming a government with a branch of leftist parties or with PASOK. The less feasible scenario points to no government being formed (again), implying that the country should call a third round of elections. Our view is that any government emerging from the elections will opt for a re-negotiation of the terms of the program and that an exit from the euro would not materialize.
- On Monday and Tuesday will take place the G-20 meeting in Los Cabos, Mexico. Several G-20 officials have said that Central Banks are ready to avoid any liquidity constraints if over the weekend the crisis intensifies. Moreover, the UK unveiled (on Thursday) measures to prevent contagion from Europe. They will start offering banks multiyear loans at below-market interest rate. Along, they will pump money into banks through repo operations.
- In the meantime, during the last weekend Spain informed to the Eurogroup its intention to seek financial assistance from euro area Member States of up to EUR100bn as a backstop to recapitalize its banking system in a pre-emptive move ahead of Greece's elections and the outcome of the stress test report on the Spanish banking sector due to Thursday 21. Previously, the IMF reported that (under the adverse scenario) capital needs would amount to EUR 40bn. The Eurogroup has agreed to provide such backstop to Spain, but there is an important lack of details in the communiqué, such as conditionality, which prevented the Spanish risk premium to decrease. Besides, the loan does not break the pernicious cycle between banks and sovereign as it increases public debt. In this context, Moody's downgraded Spain Sovereign bonds to Baa3 (negative outlook), which is one notch above speculative grade. The main reasons behind the Spanish downgrade were: limited access to financial markets, increase in Spain's debt burden and weak growth prospects. Furthermore downgrade depending on the outcome of the external audits of the Spanish banking system, the conditionality and details of the EFSF/ESM loan agreement and the strategy for the banking system's recapitalisation. Additionally, the risk of a Greek exit from the euro rise is an additional factor to consider. However, the downgrade pressure is not only limited to Spain. Beyond it, this pattern is especially intense in Belgium, Italy and Ireland according to our Credit Risk Model. Besides, France's sovereign rating remains under pressure.
- News from Spain and new concerns about Italy put peripherals' debt under pressure once more. Spanish bonds registered all-time records (6.9%), with spreads and CDSs also marking levels never seen before (close to 600). From safe-havens, the event was a new feeling about Germany as the 10Y German yield is climbing consistently over the last days while the US yield remained practically unchanged. Surprisingly, the euro almost didn't move, suggesting the 1.25 level as a good support for the eurodollar. During this week, Italy managed to sell its maximum target in debt. It sold EUR 4.5bn in 3Y, 7Y and 8Y bonds, though demand was weak and yields higher, reflecting the recent deterioration in the feeling about peripherals. In the coming week, Spain will test investors' appetite for government debt by selling bonds on Thursday.

- **High-frequency activity indicators continued to point to a deceleration path in developed countries, while data from China were somewhat better than expected**

- The latest batch of monthly activity indicators from China showed continuing growth moderation in May, with some outturns exceeding expectations. Both investment and retail sales continued to moderate, but at a slower pace than in recent months. Exports and imports surprised to the upside, resulting in a larger-than-expected trade surplus. Importantly, inflation eased by more than expected, to 3.0% y/y in May (consensus: 3.2%; BBVA: 3.3%), providing room for further policy stimulus in supporting growth in the months ahead. We expect additional 100-150bps cuts in the RRR, and at least one more 25bp interest rate cut, most likely in the Q3. Despite of weaker than expected growth outturns in the first half of the year, growth momentum is expected to improve in the second half of the year.
- In the eurozone, real economic data confirmed the slowdown in economic activity at the start of the 2Q12. The Industrial production in the eurozone fell by 0.8% in April, with the largest decreases in Portugal (-6.5%), Germany (-2.0%) and Italy (-1.9%), and the highest increase in the Netherlands (+2.9%). In France, manufacturing production fell (-0.7%), but total industry recovered, gaining 1.5% m/m. The lower growth has also reflected on inflation, which eased in all countries in May. Eurozone inflation was confirmed at 2.4% y/y (as expected), while falling by 0.1% on the month. In Germany, the rate fell to 1.9% y/y, as expected too, with the HICP at 2.2% (revised up by 0.1pp), in France it eased to 2% y/y, with HICP at 2.3%; while in Italy the first estimate was confirmed, with inflation around 3.2% y/y (HICP at 3.5%)
- In the US, activity figures in the 2Q continued showing moderation. Retail sales fell by -0.2% m/m in May from a downwardly revised -0.2% in April. Along, last week's initial jobless claims surprised to the upside, 386k from upwardly revised 380k in the previous week. Meanwhile, CPI declined slightly more than expected in May, down 0.3% following no change in April. Headline inflation had been relatively strong on a monthly basis throughout the first quarter but it is not reflective of falling energy prices. On a y-o-y basis, headline inflation dropped from 2.3% in April to 1.7% in May, the lowest rate in more than a year. Despite the recent swings in headline inflation, core prices held steady at 0.2% m/m for the third consecutive month. Regarding next week FOMC's meeting, further action from the FED is unlikely. The FED needs to see more data before coming to a conclusion on labor market conditions. The implementation of further QE would only be justified before severe market conditions and thus it is unlikely for the time being. However, if conditions in Europe deteriorate, the FED could consider other measures (extension of operation twist or a new program).
- In Mexico, economic activity may moderate a bit in the 2Q12 but still remaining strong. Over the 1Q12, Mexican GDP growth was mainly driven by private demand, household spending, business investment and exports. The information available for the second quarter suggests that the Mexican economy is performing well though in a somewhat slower pace if compared with the 1Q12.

Many relevant events will take place in the next few days: Greek elections on June 17. On Monday and Tuesday the G-20 leaders will attend to the Summit in Los Cabos (Mexico). Also the FOMC will hold its two-days meeting on June 19 and 20, in which the FED will deliver its summary of economic projections. On Thursday, Eurogroup will hold its meeting. On the same day it is expected to be finalized the stress test for the Spanish banking system by the two independent auditors; and the Spanish Treasury will hold a bond auction. Lastly, on Friday, the German Chancellor, the French president and the Italian Prime Minister will gather with the Spanish President in Rome.

Calendar: Indicators

Eurozone: Flash EC Consumer Confidence (June, June 21st)

Forecast: -19.4

Consensus: -19.8

Previous: -19.3

We expect consumers' confidence to remain broadly stable in June, after improving slightly in the previous month but remaining clearly below its long-term average (around one standard deviation). Nevertheless, the most recent surge of financial strains could have weighed on consumers' confidence, so a large decline in June should not be ruled out. In addition, this indicator could remain at a similar level to that registered in Q1, when households' spending remained resilient (0% q/q in Q1), but retail sales contracted more than expected in April and suggest that private consumption could fall again in Q2. Overall, these figures, combined with increasing uncertainty surrounding the European financial crisis and the worsening labour market, point to a pessimistic outlook for private consumption in coming quarters.

Eurozone: Flash PMI Composite (June, June 21st)

Forecast: 45.8

Consensus: 45.5

Previous: 46.0

We expect the composite PMI to remain relatively stable in June, after the significant fall registered in previous months as a consequence of renewed strains in the eurozone. These figures mean a rapid reversion of PMI levels, after improving in Q1, towards those registered at the end-2011 when the GDP fell by -0.3% q/q. Across sectors, we also expect both manufacturing and service PMIs to remain broadly stable, although the outlook remains gloomy as slowing global demand could end weighing on the former and depressed domestic spending on the latter. Nonetheless, increasing concerns about the situation in periphery countries could end up weighing more than anticipated on confidence. Our short-term MICA model estimates a slight contraction of around -0.1% q/q in Q2-12, although it is too early to draw conclusions with still limited hard indicators for the current quarter, while risks continue to be tilted on the downside.

US: Housing Starts and Building Permits (May, June 19th)

Forecast: 720K, 725K

Consensus: 725K, 730K

Previous: 717K, 715K

Recent trends in housing activity have been positive, and new home starts and permits are both expected to increase slightly in May. The homebuilder confidence index for the month jumped to the highest level of the recovery, suggesting that current conditions improved significantly from April. However, the latest weakness in consumer data and the discouraging labor market conditions may limit housing activity in May. Building permits, which offer a leading look at the housing sector, dropped in April and indicate that gains in new home starts may be minimal.

US: FOMC Meeting Announcement (June, June 20th)

Forecast: 0.25%

Consensus: 0.25%

Previous: 0.25%

The latest FOMC statement and minutes had noted a slightly more centrist committee with lower probability of quantitative easing. However, increasing uncertainties stemming from the situation in Europe and the data released throughout the intermeeting period may influence more immediate action. Recent speeches from Fed presidents highlight mixed responses to the extremely weak labor market data, presenting a more divided committee compared to the meeting minutes. The probability of extending Operation Twist, which expires this month, has increased significantly and quantitative easing remains an option, depending on whether the weak trends continue throughout the next few months. The more likely scenario would be an extension of OT. While this would have only a small impact on rates and economic activity, it could be a tailwind to financial markets since the policy action would indicate that the Fed is ready to act whenever it is needed. With 10-year rates at all-time lows, it will be difficult, if not impossible, to stimulate the economy further with monetary policy unless the Fed gets creative.

Taiwan: Export Orders (May, June 20th)

Forecast: -2.2% y/y

Consensus: -3.0% y/y

Previous: -3.5% y/y

As a 3-month leading indicator of Taiwan's exports, export orders will be watched for further signs of weakening external demand, both for Taiwan and for the region. April export orders were disappointing (-3.5% yoy), and suggest that near-term external demand might remain sluggish, despite a surprisingly encouraging export outturn for China in the month of May (+15.3% y/y). We expect Taiwan's export orders to decline again, but at a decelerating rate. Export orders to China should begin to stabilize, especially following stimulus policies to support growth. The Taiwanese central bank will likely keep its wait-and-see approach to further interest rate cuts at its next quarterly policy meeting, a day after the export orders release.

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	0.28	1	-1	-10
		10-yr yield	1.58	-6	-18	-137
	EMU	3-month Euribor rate	0.66	0	-2	-84
		2-yr yield	0.07	3	0	-144
		10-yr yield	1.44	11	-3	-152
Exchange rates (changes in %)	Europe	Dollar-Euro	1.262	0.8	-0.7	-11.8
		Pound-Euro	0.81	-0.2	1.1	-8.6
		Swiss Franc-Euro	1.20	0.0	0.0	-1.1
	America	Argentina (peso-dollar)	4.50	0.2	1.1	9.8
		Brazil (real-dollar)	2.05	1.1	2.3	28.1
		Colombia (peso-dollar)	1786	0.5	-0.5	-0.4
		Chile (peso-dollar)	499	-0.6	-0.3	5.7
		Mexico (peso-dollar)	13.90	-0.1	1.0	16.8
		Peru (Nuevo sol-dollar)	2.67	-0.3	-0.1	-3.3
	Asia	Japan (Yen-Dollar)	78.69	-1.0	-2.0	-1.7
		Korea (KRW-Dollar)	1165.75	-0.8	0.0	7.4
		Australia (AUD-Dollar)	1.005	1.3	1.4	-5.4
Comm. (chg %)		Brent oil (\$/b)	98.0	-1.5	-12.3	-13.5
		Gold (\$/ounce)	1627.6	2.1	5.7	5.7
		Base metals	516.0	0.6	-1.5	-14.3
Stock markets (changes in %)	Euro	Ibex 35	6734	2.8	1.8	-33.6
		EuroStoxx 50	2185	1.9	0.4	-21.1
	America	USA (S&P 500)	1337	0.8	0.9	5.1
		Argentina (Merval)	2191	-0.3	1.4	-33.0
		Brazil (Bovespa)	55413	1.8	-0.8	-9.2
		Colombia (IGBC)	14025	-0.1	-3.5	0.0
		Chile (IGPA)	20614	-1.4	-1.2	-6.1
		Mexico (CPI)	37464	0.4	-0.1	7.0
		Peru (General Lima)	20708	-1.2	-0.7	4.1
		Venezuela (IBC)	243839	1.4	3.2	201.5
	Asia	Nikkei225	8569	1.3	-2.6	-8.4
		HSI	19234	4.0	-0.1	-11.3
Credit (changes in bps)	Ind.	Itraxx Main	181	4	2	70
		Itraxx Xover	702	6	-40	293
		CDS Germany	106	-2	10	66
	Sovereign risk	CDS Portugal	1037	-72	-101	245
		CDS Spain	600	13	62	311
		CDS USA	49	0	7	---
		CDS Emerging	287	-17	-24	56
		CDS Argentina	1226	-135	80	597
		CDS Brazil	152	-11	-2	36
		CDS Colombia	141	-10	-3	30
		CDS Chile	119	-3	5	44
		CDS Mexico	139	-12	-7	27
		CDS Peru	157	-6	2	7

Source: Bloomberg and Datastream

Weekly Publications

Country	Date	Description
USA	14/06/2012	➤ U.S. Economic Watch. Structural Series: Transportation Infrastructure Closing the Funding Gap via Public-Private Partnership
	14/06/2012	➤ U.S. Inflation Flash. Falling Gas Prices Drag Down Headline Inflation in May Headline inflation dropped 0.3% MoM in May following no change in April. Energy index fell 4.3%, led mostly by a 6.8% decline in gas prices. Core prices increased 0.2% for the third consecutive month
	11/06/2012	➤ U.S. Weekly Flash: "Fedspeak Mixed Leading up to June FOMC Meeting" The latest speeches from the Federal Reserve suggest mixed responses to extremely weak labor market data (Chinese version) (Spanish version)
EMU	14/06/2012	➤ Europe Flash: "Eurozone inflation decelerates somewhat faster than expected" Inflation eased in May for the second month in a row to 2.4% y/y, after remaining broadly stable at 2.7% y/y in the first quarter. We expected a more moderate slowing.
Spain	13/06/2012	➤ Consumption Outlook. First Half 2012 Weak fundamentals mean that consumption, especially of durable goods, is expected to decline.
	13/06/2012	➤ Flash España: "IPC en mayo" El IPC de mayo confirma la desaceleración esperada de la inflación debido, fundamentalmente a la moderación del crecimiento de los precios de la energía y los alimentos no elaborados.
	12/06/2012	➤ Situación Madrid. Primer semestre 2012 La economía madrileña experimenta un menor impacto de la crisis por los menores desequilibrios y la mayor rapidez en el ajuste. A largo plazo, resulta fundamental mantener el esfuerzo educativo. Presentación de "Situación Madrid. Primer semestre 2012"
	11/06/2012	➤ Flash España: "Compraventa de viviendas en abril de 2012" En el mes de abril se vendieron 21.551 viviendas, un 0,5% menos que en el mes anterior, tras corregir la serie de variaciones estacionales y efectos de calendario (cvec).
Latin America		
Chile	14/06/2012	➤ Banco Central mantiene tasa de referencia en 5% y sesgo neutral Se menciona que la actividad se ha desacelerado en línea con lo esperado y que los registros y expectativas de inflación continúan anclados en torno a la meta.
Mexico	14/06/2012	➤ Mexico GDP Flash. 1Q12 GDP: growth based on private spending and exports, disposable income and access to financing Growth in the 1Q12 rested in private demand, household spending and business investment and in exports (Spanish version)
	13/06/2012	➤ Flash Inmobiliario México. La demanda de vivienda crece con fuerza, ¿Por qué la oferta no la sigue? En los primeros cuatro meses del año, el monto de financiamiento en créditos hipotecarios otorgados por el sistema financiero ha crecido 34% en términos reales
	13/06/2012	➤ Real Estate Flash Mexico. Construction GDP grew by more than 4%, in line with our forecast In line with our forecast set out in the previous edition of this Real Estate Flash, construction GDP grew by more than 4%, although it fell short of 5% (Spanish version)
	13/06/2012	➤ Real Estate Flash Mexico. Strong growth in housing demand; why does supply not follow suit? In the first four months of the year, the volume of mortgage lending granted by the financial system grew by 34% in real terms
	11/06/2012	➤ Mexico Flash. Industrial production in April: 0.7% m/m, about the same as expected, external demand continues to pull in activity Industrial production slightly higher than expected (0.5% expected, 0.7% observed). Good performance in the manufacturing industry (1.1%) and mining lags (-0.5% m/m) (Spanish version)

Asia

- 14/06/2012 ➤ **Asia Daily Flash | 14 June 2012: Hong Kong issues measures to support liquidity in the offshore RMB market;** India's inflation rises; Philippines holds rates
The Hong Kong Monetary Authority unveiled two new measures today to support liquidity in the offshore RMB market.
- 14/06/2012 ➤ **India Flash: Benign core inflation builds case for policy easing next week**
India's wholesale price inflation rose in May, to 7.55%y/y (Consensus: 7.5%) from 7.23% in April driven mainly by higher food and fuel prices.
- 13/06/2012 ➤ **Asia Daily Flash | 13 June 2012: A proposed change to Hong Kong's peg makes a stir; Fitch affirms** Australia's AAA rating; Thailand holds interest rates
In newly published academic paper the former head of the HKMA says the authorities should consider eventually delinking Hong Kong's currency peg from the USD, causing a stir
- 12/06/2012 ➤ **Asia Daily Flash | 12 June 2012: India's IP growth remains flat; Indonesia keeps interest rates unchanged;** IMF praises Japan's economic resilience
India's industrial production growth came in below expectations for April (0.1% y/y vs. consensus: 1.1%), but up from a -3.2% contraction in March.
- 11/06/2012 ➤ **Asia Daily Flash | 11 June 2012: China indicators show growth moderation and scope for policy stimulus;** China's monetary and credit data picks up; Singapore's exports increase
Positive news from Europe on Spain's banking package and somewhat better-than-expected data outturns in China lifted sentiment today.
- 11/06/2012 ➤ **China Flash: May indicators point to gentle growth moderation and scope for more policy stimulus**
The latest batch of monthly activity indicators for May, released over the weekend, show continuing growth moderation, with some outturns exceeding expectations.

Publications on June 15, 2012 to 10:00, Madrid time

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