



# Weekly Observatory

March 16, 2009

## Financial markets: surprising recovery in market sentiment

Stock markets experienced an unexpected recovery over the week, triggered by some positive announcements by US banks and then reinforced by investors covering short positions, which had reached an extreme level in last weeks. Issuance of guaranteed debt by banks increased sharply too, taking advantage of the window of opportunity offered by this recovery. Lower risk aversion and the continued concerns about supply of government bonds led to an increase in bond yields, and some appreciation of the Euro. For further information, see [Flow Watch](#) (in Spanish).

## United States: Retail sales increased across various sectors; yet, we expect PCE to remain weak.

February's retail sales excluding autos increased 0.7%, reflecting a widespread increase across various sectors. However, motor vehicle dealers saw a decrease of 4.9%. The report suggests that demand for certain goods has improved compared to the 4th quarter, but we still expect a decline in overall consumption spending mainly because durable goods spending continues to decrease at a high rate. This week, we are forecasting that February's headline inflation will come in at 0.3% due higher gasoline prices; however, we expect core inflation to remain steady at 0.2%. Finally, given that downward risks to economic growth remain, we believe that the Federal Reserve will keep its target interest rate constant in Wednesday's meeting. For further information, see [US Weekly Observatory](#).

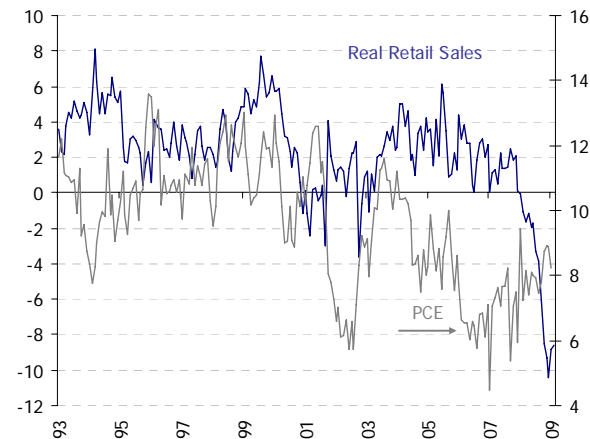
## Euro area: Very negative data for exports and industrial sector

Very negative data on real activity were released this week. Industrial production in Germany and France fell in January by monthly rates of -7.5% and -3.1%, respectively, much more than expected. Industrial orders also plunged in Germany, while exports dropped both in Germany and France. On a less negative note, retail sales for the euro area edged up by 0.1% in January, broadly as expected. All in all, we have revised our forecast for growth in the first quarter from -1% to -1.6% for the area. On prices, Germany and France inflation for February confirmed the flash release, with core inflation stable in Germany and accelerating in France while producer prices in the euro area decelerated rapidly in January. Labour costs also decelerated in 2008 Q4, but moderately and still remain high at 3.8%. For further information, see [Europe Weekly Observatory](#).

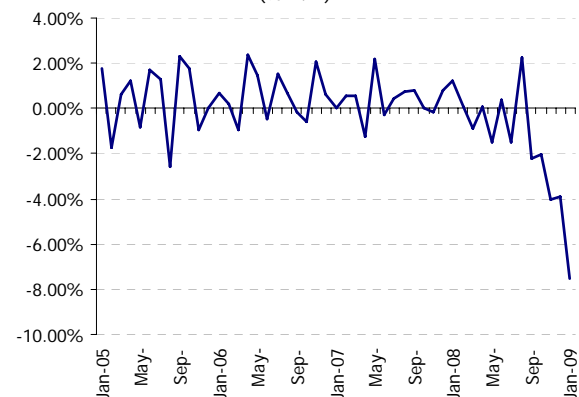
## Latin America: activity in Brazil plummeted on Q408

Brazil released GDP data for 4Q08, which results into a quarter-to-quarter fall of 3.6%, worse than expectations. Both the drastic deceleration of activity and the parallel drop in inflation has led the Central Bank of Brazil to slash the SELIC by 150 bps, currently standing at 11.25%. These same considerations are also at play in Chile, where the monetary authority undertook a bold rate cut of 250 bps, to leave the reference rate at 2.25%.

**Real Retail Sales & PCE**  
(12-month % change)

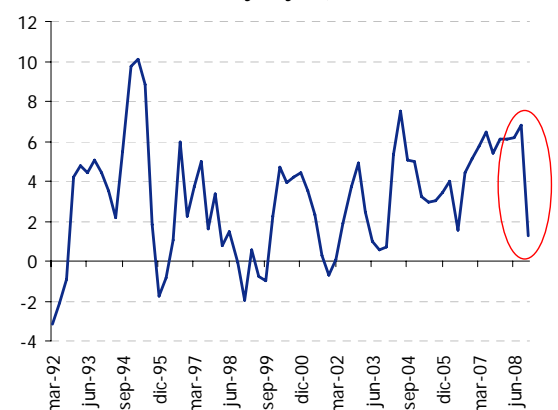


**Germany: Industrial production index**  
(% m/m)



Source: Eurostat

**Brazilian GDP**  
(y-o-y %)



Lower inflationary pressures generalize throughout the region. Thus, recent trade data confirms the retreat of international commerce in the region, both through exports and imports. As for the events next week, we highlight the monetary policy meeting in Mexico (we expect a rate cut of 25 bps), as well as monthly GDP data for January in Peru. For further information, see [Latin America Weekly Observatory](#).

### Asia: Some positive dataflow; underlying weakness remains

Exports and industrial output slowed in China but there are positive signs gaining traction, as urban fixed asset investments, broad money and credit growth surged in the first two months of 2009. Some positive dataflow came also from Japan's revision of Q4 2008 marginally upwards and better-than-expected labor force report in Australia as well as industrial production in India. A closer look at the details, however, still point to weakening growth momentum ahead. On monetary policy, Bank of Korea left its policy rate unchanged in a surprise move. This week, the financial markets will focus on Bank of Japan's monetary policy meeting over March 18-19th and Singapore's non-oil domestic exports release on the Asian data front. For further information, see [Asia Weekly Observatory](#)

### Spain: inflation numbers in line with our estimates

This week's data brought the CPI breakdown for the month of February. On the one hand, headline inflation dropped to 0.7 percent year on year from 0.8 percent in January (in line with our forecast). On the other hand, core inflation fell to 1.6 percent year on year from 2 percent last month, mostly due to a sharp decline in non-energy industrial goods, although inflation in services also kept its downward path for the sixth month in a row. We maintain our forecast of 0.2 percent inflation in 2009.

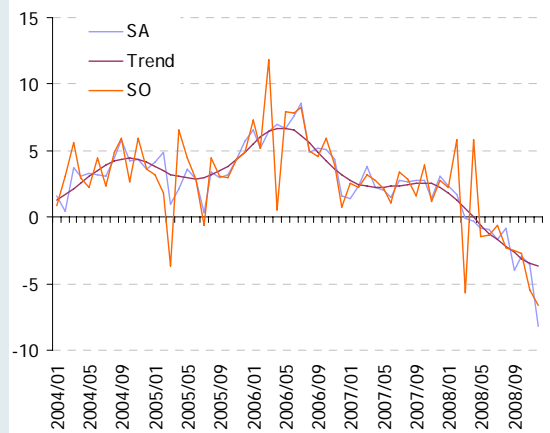
### México: fiscal data reflect the anticyclical policies

In february inflation grew 0.22% (6.2% vs. 6.28% y/y in January) while core inflation grew 0.49% (5.78% vs. 5.76% y/y in January). The current juncture is complex because core inflation might be higher than CPI inflation by end of 2009 and in 2010, because of an asymmetric shocks (negative tradable goods prices vs. broader output gap). Gross Fixed Investment grew 4.9% y/y in 2008, investment in Equipment and Machinery increased 12.9% while construction reduced (-) 0.4%. This week the Central Bank could announce a further cut in the regulatory interest rate (-25 bp) since activity risk balance has deteriorated over the last month: we are forecasting a mayor reduction in industrial production for January (-10% y/y). and in the aggregate demand for Q4-08 (-2.3%y/y). For further information see [Mexico Weekly Observatory](#) (in Spanish).

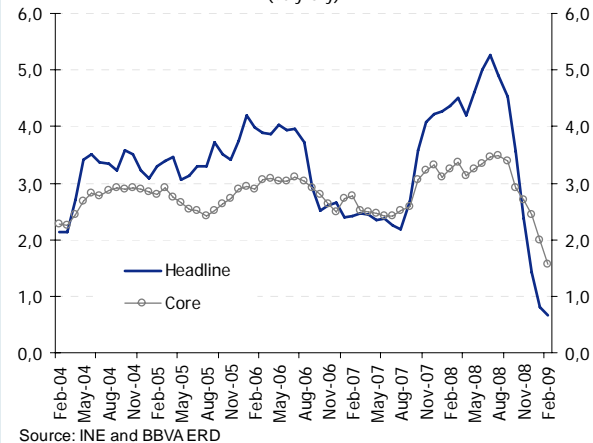
### Commodities: oil prices remain stable ahead of OPEC's meeting

Oil prices were practically stable this week ahead of OPEC's meeting which will be hold this weekend. Another supply cut is expected (the fourth since September), although this view was challenged during the week by Saudi Arabian comments about the importance of enforcing previous cuts before announcing a new one. For further information, see [Commodities Observatory](#).

Industrial Production in Mexico

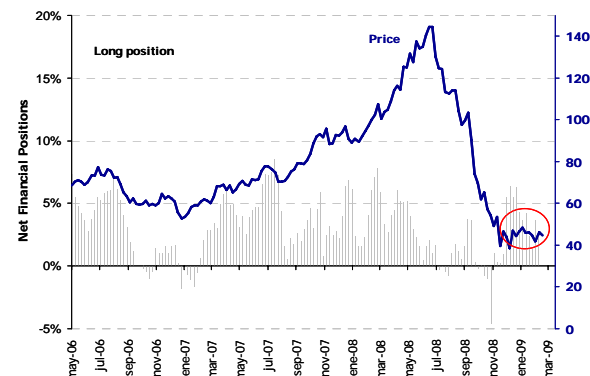


Spain: inflation (% y-o-y)



Source: INE and BBVA ERD

Brent Prices and Non-Commercial Positions



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