

Global Weekly Flash

The European crisis intensifies

- **Fears of a potential Greek exit from the eurozone continue to dominate markets as Greece will hold new elections on June 17 and news arrive of accelerated deposit withdrawals**

- Risk sentiment continued to deteriorate during the week as fears on a potential exit from the eurozone by Greece and uncertainty on its possible impact mounted further. Additionally, over the last week, fears surfaced of a bank run on Greek banks. In Spain Moody's lowered the ratings of several banks and rumors spread around deposit withdrawals from Bankia (later dismissed) adding to the gloomy outlook.
- Eurozone risk spreads widened (eg, the Spanish risk premia reached its all time high and momentarily surpassed the 500bp threshold), safe-haven yields continued to drop as investors shy away from risk (German 10y bond yields drop to all time lows) and the euro's resilience up to this week began to show signs of weakening as the euro dipped below 1.27. Up to now, interest rate differentials and only moderate have explained the strength of the euro.
- In the meantime, European policymakers seem to be trying to change Greek voters' perceptions on the upcoming election: it is not about rejecting the bailout conditions; it is about euro area membership. In this sense, the European Commission and the ECB are preparing a contingency plan in case Greece leaves the eurozone, while the President of the ECB has acknowledged for the first time that Greece could leave the euro and the ECB temporarily. In addition, the ECB announced that some Greek banks will be temporarily restricted from access to its liquidity line (until their recapitalization process is finalized) and will have to tap the Emergency Liquidity Assistance (ELA) from the Greek central bank to obtain funding.
- Against the backdrop of rising tensions, the ECB is conducting a comprehensive review of all its policy tools to assess the effectiveness of its non-standard measures: the bond-buying programme (SMP) and the long-term refinancing operations (LTROs). The review is scheduled to be completed in June or July so it is unlikely that the ECB may consider taking any additional policy steps before. Besides, the ECB is convinced that they cannot solve the "fundamental problems"; they can "only buy time" and there is a "limit to how much time" can be bought.

- **Positive surprises outside the eurozone**

- In the US, housing data and industrial production rebounded in April fueling optimism. Housing starts rose 2.6% m/m to a seasonally adjusted annual rate of 717K from an upwardly revised 699K pace in March and above expectations (consensus: 685K). Yet, the rebound is still mainly rests on multi-family starts. Meanwhile, industrial production also came in stronger-than-expected, rising 1.1% m/m (vs. 0.6% anticipated) mainly driven by a strong increase in automobiles and parts production (3.9%). Manufacturing output rebounded (rising 0.6% m/m) after dropping 0.5% in March. FOMC Minutes revealed little additional information as increasing international financial instability in the time since the last FOMC meeting has become more of a driver of the Fed reaction function than any particular element of the minutes. Chairman Bernanke and other FOMC participants have continually stated that the Fed will act if economic conditions deteriorate. Thus, it is clear that the Federal Reserve is closely monitoring conditions in financial markets and developments in Europe to gauge if downside risks become "great enough". UK's May Inflation Report also showed increased concerns over the severe downside risks stemming from a potential euro area break-up. As a consequence, it indicated a bias to loosen monetary policy in spite of persistently elevated inflation.
- Elsewhere, a positive outturn for Japan's Q1 GDP beat expectations and points towards an ongoing rebound. Japan's 1Q GDP data release shows that the economy expanded by an annualized rate of 4.1% y/y in the first quarter (consensus: 3.5%), boosted by private consumption, public investment, and exports. Looking ahead, we expect Japan to continue its recovery in the coming quarters, and we expect GDP growth in 2012 to reach about 2%.

- Mexican economy also surprise positively. The Mexican economy grew 1.3% qoq in seasonally adjusted series in 1Q12, above our forecast of 0.7% qoq. The growth in annual terms stood at 4.7%, implying a significant improvement over the previous quarter (3.9%). The positive surprise in the first quarter prints an upward bias to estimates of 2012 and 2013, at this time by 3.7% and 3.0%. This report confirmed the Banxico inflation report where the Bank increased its growth range forecast for 2012 slightly to 3.25%-4.25% from 3%-4%. Banxico's inflation report highlighted that the inflation will remain between 3.0% and 4.0% during 2012 and 2013. In our opinion, last reports support the perspective of monetary pause. Beside the Central Bank of Chile kept its main reference rate at 5% despite higher growth signalling uncertainties about the external environment, especially about the resolution of the European debt crisis.
- In contrast, eurozone GDP remained flat in Q1 12 driven by a larger than projected rebound in Germany (0.5% q/q vs. 0.1% anticipated) that compensated a negative surprise in Italy (-0.8% q/q vs. -0.6% anticipated). Our forecasts suggest that Q1 performance was supported by a slightly positive contribution of net exports, and weakness of domestic demand. This forecast was reinforced by the small trade surplus in March.

Next week investors will be paying attention to the extraordinary EU council meeting on 23. We hope that this event would help to introduce growth-friendly measures along with the fiscal compact. Besides, next week in the eurozone will be published the PMI and the consumer confidence for may, while in the US Durable orders and housing data for April will keep investor attention.

Calendar: Indicators

Eurozone: Flash EC Consumer Confidence (May, May 22nd)

Forecast: -20.0

Consensus: -20.4

Previous: -19.9

We expect consumers' confidence to remain broadly stable in May, after having fallen in the previous month thus interrupting the improvement seen earlier this year. Though the GDP detailed breakdown for Q1 is not yet available, the flash estimate and retail sales figures were in line with our forecasts that point to a more resilient private consumption at the beginning of the year, although falling slightly. But consumer confidence remains clearly below its historical average, and combined with increasing uncertainty surrounding the European financial crisis and the worsening labour market it suggests that private consumption should remain very subdued in coming quarters. However, the most recent surge of financial strains could have weighed in consumers' confidence, so a large decline in May should not be ruled out.

Eurozone: Flash PMI Composite (May, May 24th)

Forecast: 46.5

Consensus: 46.5

Previous: 46.7

We expect the composite PMI to remain relatively stable in May, after the significant fall registered in the previous month 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. 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 set of information for the current quarter.

US: Existing Home Sales (April, May 22nd)

Forecast: 4.55M

Consensus: 4.60M

Previous: 4.48M

Existing home sales are expected to increase only slightly in April as tight credit and weak employment conditions continue to weigh on homebuyer demand. Housing affordability is near an all-time high as a result of the large supply of distressed properties, yet the volume of mortgage applications was relatively unchanged in April. Foreclosures still account for more than 7% of total homes, down from a peak of 10.8% for the recovery period. In general, sales of existing homes have been moderating on a YoY basis since mid-2011, and we expect this trend to accelerate as the year progresses.

US: Durable Goods Orders, Ex Transportation (April, May 24th)

Forecast: 2.0%, 1.0% m/m

Consensus: 1.0%, 1.0% m/m

Previous: -4.0%, -0.8% m/m

Durable goods orders declined significantly in March but are expected to rebound in April with a boost from the auto sector. Despite initial estimates for flat output throughout most of the first quarter, the latest industrial production data reflected upward revisions to some months as well as a jump in April's data, with auto production a primary driver. Various manufacturing reports have indicated continued growth in new orders but at a slightly slower pace compared to the previous months. Given the usual volatility in the data, we expect that durable goods orders will recover from weakness in March.

Taiwan: export orders (April, May 21st)

Forecast: -1.96% y/y

Consensus: 0.02% y/y

Previous: -1.58% y/y

Taiwan's export performance is closely watched as a bellwether of regional export trends. April exports contracted by worse-than-expected -6.4% yoy, and production growth trends are declining, as seen in moderating PMI outturns. Looking ahead, we expect that April export orders to show a further decline due to weaker external demand. This is also in line with China's recent disappointing macro outturns and moderation in domestic demand, including a leveling off of processing components imports could weigh on the Taiwan'.

Markets Data

			Close	Weekly change	Monthly change	Annual change
Interest rates	(changes in bps)	US	3-month Libor rate	0.47	0	21
			2-yr yield	0.30	4	-21
			10-yr yield	1.73	-11	-141
		EMU	3-month Euribor rate	0.68	-1	-75
			2-yr yield	0.05	-4	-172
			10-yr yield	1.43	-9	-163
Exchange rates	(changes in %)	Europe	Dollar-Euro	1.272	-1.5	-3.0
			Pound-Euro	0.80	0.0	-1.9
			Swiss Franc-Euro	1.20	0.0	-0.1
		America	Argentina (peso-dollar)	4.45	0.3	1.1
			Brazil (real-dollar)	2.01	2.0	6.8
			Colombia (peso-dollar)	1812	2.8	2.1
			Chile (peso-dollar)	503	3.3	2.9
			Mexico (peso-dollar)	13.76	1.4	4.4
			Peru (Nuevo sol-dollar)	2.67	0.4	0.5
		Asia	Japan (Yen-Dollar)	79.32	-0.8	-2.4
			Korea (KRW-Dollar)	1172.73	2.3	3.1
			Australia (AUD-Dollar)	0.987	-1.5	-4.7
Comm.	(chg %)		Brent oil (\$/b)	107.4	-4.3	-9.0
			Gold (\$/ounce)	1590.9	0.7	-3.1
			Base metals	521.8	-1.5	-2.6
Stock markets	(changes in %)	Euro	Ibex 35	6576	-6.0	-7.1
			EuroStoxx 50	2156	-4.4	-7.4
		America	USA (S&P 500)	1310	-3.2	-5.5
			Argentina (Merval)	2122	-7.9	-10.0
			Brazil (Bovespa)	54270	-8.7	-13.9
			Colombia (IGBC)	14294	-4.8	-5.5
			Chile (IGPA)	20708	-3.8	-4.3
			Mexico (CPI)	37261	-4.2	-5.3
			Peru (General Lima)	20652	-4.7	-11.3
			Venezuela (IBC)	236212	-9.1	3.9
		Asia	Nikkei225	8611	-3.8	-10.9
			HSI	18952	-5.1	-8.8
Credit	(changes in bps)	Ind.	Itraxx Main	182	24	39
			Itraxx Xover	754	68	79
		Sovereign risk	CDS Germany	98	10	20
			CDS Portugal	1161	86	47
			CDS Spain	551	34	56
			CDS USA	43	2	13
			CDS Emerging	317	47	47
			CDS Argentina	1190	199	126
			CDS Brazil	157	24	27
			CDS Colombia	146	25	27
			CDS Chile	118	15	20
			CDS Mexico	147	25	20
			CDS Peru	158	25	28

Source: Bloomberg and Datastream

Weekly Publications

Country	Date	Description
USA	05/16/2012	<p>> FOMC Minutes April 25</p> <p>Minutes reveal little additional information to inform our view of the FOMC's desires. FOMC members opt for all two-day meetings henceforth, more time needed to discuss</p>
	05/15/2012	<p>> Lower Energy Costs Limit Headline Inflation in April</p> <p>Headline inflation was unchanged in April, mostly due to a 2.6% drop in gas prices. Core prices increased 0.2% and held steady at 2.3% on a YoY basis</p>
	05/14/2012	<p>> U.S. Weekly Flash. Trade Balance Deteriorates Despite Improvements in Underlying Demand</p> <p>The international trade balance worsened in March to -\$51.8bn from an improved -\$45.4bn in February, closing out 1Q12 as one of the weakest trading quarters throughout the recovery period</p> <p>Chinese version</p>
EMU	05/16/2012	<p>> Europe Flash: "Eurozone GDP flat in Q1-12, as expected, with a positive surprise in Germany"</p> <p>Eurozone activity remained flat in the first quarter of the year, as expected, driven by a larger than projected rebound in Germany that compensated a negative surprise in Italy.</p>
	05/16/2012	<p>> Europe Flash: "Headline inflation eased by 0.1pp to 2.6% y/y in April, while core inflation remained stable at 1.9% y/y, as expected"</p> <p>Inflation eased to 2.6% y/y in April, as expected, after remaining broadly stable at 2.7% y/y in the first quarter.</p>
Spain	05/17/2012	<p>> Flash España: "Contabilidad Nacional Trimestral del 1T 2012"</p> <p>Tal y como se adelantaba en el último número de nuestra revista "Situación España", la economía española entró en recesión técnica en el 1T12.</p>
Latin America	05/16/2012	<p>> Situación Latinoamérica. Segundo trimestre 2012</p> <p>América Latina crecerá 3,7% en 2012 y 3,8% en 2013, impulsada por la demanda interna. Las autoridades deben aprovechar la coyuntura para aumentar los amortiguadores de política monetaria y fiscal.</p> <ul style="list-style-type: none"> • El crecimiento mundial se recuperará gradualmente en 2012 del bache del cuarto trimestre de 2011. La recuperación será más pronunciada en Asia. • América Latina crecerá 3,7% en 2012 y 3,8% en 2013 impulsada por la demanda interna y los altos precios de las materias primas. • Se mantendrá un cauteloso sesgo restrictivo de los bancos centrales, salvo en Brasil. Deberán equilibrar las presiones inflacionistas y la fuerte demanda interna frente a la resistencia de los flujos de entrada de capitales y la incertidumbre exterior. • Los riesgos para el crecimiento en la región se centran en el entorno exterior, especialmente un recrudecimiento de la crisis Europea. <p>"Latam: Convergencia al crecimiento potencial". Presentación de "Situación Latinoamérica. Segundo trimestre 2012"</p>
Brazil	05/17/2012	<p>> Brazil Economic Outlook. Second Quarter 2012</p> <p>Government and Central Bank act to permanently bring interest rates down.</p> <ul style="list-style-type: none"> • Government and Central Bank act to permanently bring interest rates down. • Growth and inflation have been surprising to the downside, but we expect both to pick up following the adoption of a lax monetary policy. • A more depreciated real will impact growth and external accounts positively and inflation negatively. • The transition to a new macroeconomic equilibrium based on lower interest rates and a more depreciated exchange rate brings challenges.
Chile	05/15/2012	<p>> Situación Chile. Primer trimestre 2012</p> <p>En Chile, reducimos la proyección de crecimiento para 2012 de 4,5% a 4%, principalmente por un peor entorno externo.</p> <ul style="list-style-type: none"> • La economía mundial se desacelera. Seguirá liderada por las economías emergentes. El crecimiento se recuperará en la segunda mitad de 2012. • En Chile, reducimos la proyección de crecimiento para 2012 de 4,5% a 4%, principalmente por un peor entorno externo. • La inflación alcanzaría a 3,1% al cierre de 2012, pero la convergencia a la meta del banco central será lenta y solo podrá alcanzarse al final del año. • En política monetaria, no vemos espacio para recortes significativos a la tasa de referencia, y esperamos solo una baja de 25 pb durante el primer trimestre del año. • La materialización de un escenario de riesgo encontraría a Chile en buen pie, con capacidad de conducir políticas monetaria (principalmente) y fiscal expansivas, y con un impacto menor al de la pasada recesión.

Colombia	05/15/2012	<p>> Colombia Economic Outlook Second Quarter 2012 Colombia's economy will grow at 5% in 2012 in a healthy slowdown in which growth will gradually converge closer to its potential</p> <ul style="list-style-type: none"> • The global economy will pick up steadily in 2012 thanks to higher growth in Asia, while Europe will suffer a slight recession • Inflation will remain stable after a good first quarter that has put a check on expectations • The Central Bank will keep an eye on local and global indicators, and if there are any signs of global return to normal conditions, it will move to a more neutral stance <p>(Spanish version) Presentación "Situación Colombia. Segundo trimestre 2012"</p>
Peru	05/15/2012	<p>> Flash Perú: Actividad creció 5,6% interanual en marzo Si bien este resultado fue algo menor que el esperado (BBVA y Consenso: 6,0%), siguió reflejando un importante dinamismo económico.</p>
Mexico	05/17/2012	<p>> Mexico Flash: 1Q12 GDP above expected (1.3% qoq vs. 0.7% estimate), which prints upward bias to 2012 In contrast to expectations based on monthly indicators, the activity increased nearly double last quarter (Spanish version)</p>
	05/16/2012	<p>> Mexico Flash: Banxico's improves its perspectives on domestic activity. The report is consistent with a monetary pause Banxico modifies slightly upward its estimate of GDP growth in 2012 from a range between 3.0% and 4.0% to a range between 3.25% and 4.25% (Spanish version)</p>
	05/16/2012	<p>> Observatorio Económico: Flexibilización del régimen de inversión y reglas operativas en el Sistema de Ahorro para el Retiro (SAR) Se incrementa el límite de inversión en Instrumentos Estructurados (IE), particularmente en sectores de Vivienda e Infraestructura</p>
	05/15/2012	<p>> Mexico Flash: Surprising housing sales in the first quarter The activity of public institutions is returning to normal, although it seems to be a significant increase. Commercial banks benefited on both fronts (Spanish version)</p>
	05/14/2012	<p>> Mexico Flash: Third positive step in a row, confirming the excellent start of the year in construction Three months out of three above 4%: construction grows by an average of 4.9%. Building, employment and unusually good cement sales figures boost the sector (Spanish version)</p>
	05/14/2012	<p>> Mexico Flash: Industrial production rebounded in March, bringing the trend of annual growth and the prospect of activity Industrial production rebounded in March and grows 1.5% mom (0.8% expected), which holds annual rate similar in terms of trend to the previous quarter (Spanish version)</p>
Asia	05/17/2012	<p>> Daily Flash Asia 17 May 2012: Upbeat Japan Q1 GDP growth data points towards an ongoing rebound; China: Wenzhou introduces new reporting guidelines for private lending; Singapore: positive surprise in exports A positive outturn for Japan's Q1 GDP, released today, helped lift sentiment, causing several Asian stock markets to rebound (Shanghai 1.4%, Taiwan 1.7%) after yesterday's heavy losses</p>
	05/16/2012	<p>> Presentation of "RMB internationalization: London's potential from Hong Kong's perspective" 1. Why is China pushing to internationalize the RMB? 2. Is HK enough? 3. London's potential role Rapporteur: Alicia Garcia-Herrero Event: Presentation of "RMB internationalization: London's potential from Hong Kong's perspective" in Chatham House and Central Policy Unit Hong Kong SAR</p>
	05/16/2012	<p>> Daily Flash Asia 16 May 2012: Indian rupee hits all-time lows on global, twin deficit concerns; China's efforts to spur consumption may get a boost; South Korea's national pension fund to invest in China's equity markets Ongoing uncertainties surrounding Greece and the euro triggered sharp selloffs in Asian equity and currency markets today</p>
	05/15/2012	<p>> Daily Flash Asia 15 May 2012: FDI inflows to China contract and the authorities seek to relax rules on foreign investors; RBA minutes show that lower growth and inflation prompted the rate cut Asian markets rallied towards the end of the day on some positive news out of Europe after days of declines.</p>
	05/14/2012	<p>> India Flash: WPI inflation rises on higher food prices, while core holds steady India's wholesale price inflation edged up by more than expected in April, to 7.2% y/y (BBVA: 7.0%, Consensus: 6.7%) from 6.9% in the previous month driven by higher food prices.</p>

05/14/2012

> **Daily Flash | Asia | 14 May 2012: Rising food prices drive up India's inflation; China, South Korea and Japan to begin talks towards a free-trade agreement**

The major news over the weekend was China decided on a 50bps cut the reserve requirement ratio following a batch of weak April data outturns on Friday.

Emerging Markets

05/18/2012

> **Country Risk Quarterly Report Second Quarter 2012**

Financial Stress relaxed somehow after the liquidity measures introduced by the ECB (LTRO)

EAGLEs

05/16/2012

> **Economic Watch: Central bank balance sheets in EAGLE countries also growing fast but different composition matters to spell out risks**

A significant increase of central bank (CB) balance sheets is a distinctive feature of the world economy since the global crisis

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