



# Weekly Observatory

February 22, 2010

## Financial markets: Fed move is just technical adjustment

Market attention focused on the Federal Reserve at the end of the week after increasing the discount rate from 0.5% to 0.75%. The Fed stated the move should not be considered as monetary policy tightening but rather a technical adjustment. However, the release at the beginning of the week of the attached minutes of the Committee meeting held on January 26-27 had also shown a hawkish mood. Despite market correction on Friday following the Fed decision, the week ends with higher stock indexes and rates due to: i) better-than-expected results (even for financial institutions with punctual exceptions), ii) improving economic data in the US, and iii) a diminishing of peripheral risk in Europe outside Greece. In fact, Portuguese and particularly Spanish auctions received significant demand from investors. Next week, market participants will again be focused on a record US auction issuance. For further information, see [Flow Watch](#).

## US: Industrial production rises for the seventh consecutive month

The industrial production report indicated that economic activity is gaining momentum, as the index rose for the seventh consecutive month in January. Furthermore, the index came in at a level 0.9% above that of January 2008, marking the first y/y rise following 21 months of declines. Even though production of autos provided a large boost by rising 5%, increases were widespread across the components of both durable and non-durable goods manufacturing, which is a positive sign for sustainability. In addition, housing starts rebounded 2.8% in January after dropping 0.7% in December in m/m terms. While these results indicate that residential construction continues to stabilize, building permits dropped 4.9%, illustrating that the recovery of residential investment will be slow. For further information, see [US Weekly Observatory](#).

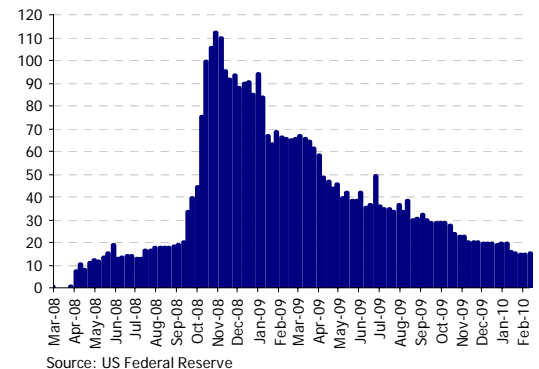
## Eurozone: upbeat indicators for industry and exports against more subdued confidence in services

From the little information released this week on the euro area, confidence indicators confirmed the more moderate mood in European business, with the composite flash PMI indicator flat in February and an increased dichotomy between an upbeat industry component and falling service confidence. Consumer confidence seemed also to worsen in February. On the real side, the trade balance for December was favorable, with strong exports during the last quarter of 2009. Our hypothesis that the slow GDP growth announced last week (0.1% q/q) was explained by very positive net exports contribution and falling domestic demand seems to be confirmed. On the ECB front, interest was focused on the election of Mr. Costancio as the next vice-president as a substitute of Mr. Papademos by next spring. For further information, see [Europe Weekly Observatory](#).

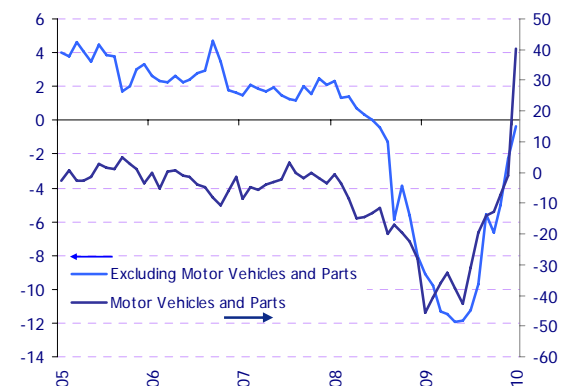
## Asia: limited data flow due to the Chinese New Year

While investors were still digesting last Friday's announcement by China of a second reserve requirement increase, they were further aggravated at the week's end as the US Fed unexpectedly rose its discount rate. Most currency and equity markets ended the week lower, despite key indicators pointing to strong economic rebounds with 4Q09 GDP beating expectations in Japan

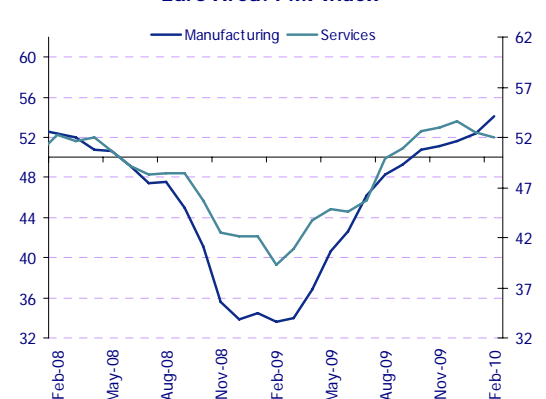
US Federal Reserve: Discount window  
(Primary credit facility, in billions of \$)



US: Industrial Production  
(y/y % chg)



Euro Area: PMI Index



and revised up in Singapore. Food prices are pushing up inflation, with India's January WPI surprising to the upside, raising prospects of further monetary tightening. We have a busy data calendar next week with 4Q09 GDP for Hong Kong, Taiwan and India, and inflation in Singapore and Japan. For further information, see [Asia Weekly Observatory](#).

### Latin America: the recovery process continues

Activity indicators are continuing to provide evidence of the recovery in the region, which in the case of Peru is reflected by an acceleration in the pace of GDP growth. The improving activity was also seen in the increase in inflation expectations in Brazil. Financial markets recorded a fall in country risk for a second week (with the exception of Venezuela) and a rise in the stock markets of Argentina, Brazil, and Chile. For further information, see [Latin America Weekly Observatory](#).

### Spain: GDP contracts in 4Q09 but shows an improved composition

The National Statistics Institute (INE) confirmed that the Spanish economy contracted by 0.1% q/q in 4Q09 (-3.1% y/y), in line with our estimates (BBVA: -0.1% q/q), which represents a lower pace of contraction compared to 3Q09 (-0.3% q/q). The lower contraction during the last quarter of 2009 is mainly explained by the performance of private consumption, equipment investment and the total exports. Household consumption, in particular, recorded its first positive growth since the beginning of the crisis (0.3% q/q). In contrast, public consumption recorded a strong contraction (-1.7% q/q), which implies that private domestic demand is progressively replacing the public sector's growth contribution and, thereby, showing a better GDP growth composition. Overall, this is consistent with our macroeconomic scenario. For further information, see [GDP Observatory](#) (in Spanish).

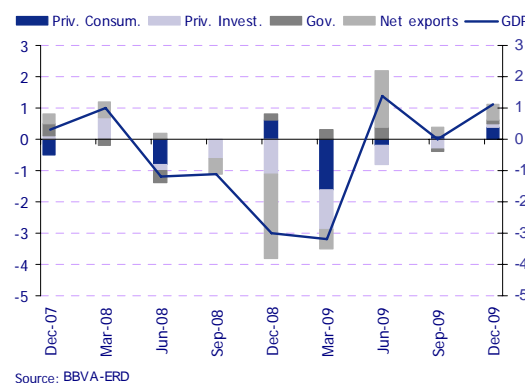
### Mexico: Banxico keeps its reference rate unchanged

In its monetary policy decision Banxico kept the reference rate unchanged at 4.5%. The assessment about economic growth reflects the uncertainty over the future recovery of the global economy. As for the domestic economic growth, no important changes in the nature of the message were stated, the perspective of recovery remains, mostly supported by the impulse of external demand. The communication kept emphasizing the transitory character of the rise in inflation during 2010, to a big extent because of the "conditions of looseness in the economy". Next week the GDP for 4Q09 will be published, we expect that the recovery started in 3Q09 will continue with a q/q growth of 1.1% (-2.9 y/y), the bi-weekly inflation for February will also be published; it is relevant to continue tracking the effects of the new fiscal changes. For further information, see [Mexico Weekly Observatory](#) (in Spanish).

### Commodities: Oil and metals, up; commodities, down

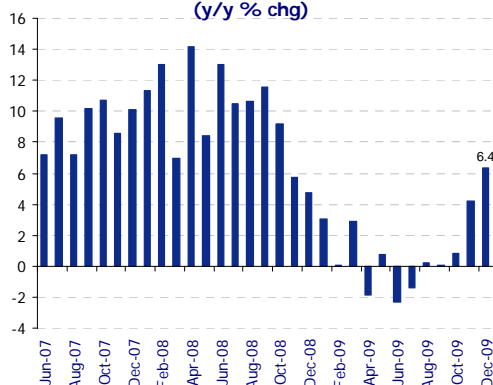
Commodity prices displayed mixed results this week, with oil and metal prices moving up following the positive tendency displayed by equity markets. Agriculture prices, however, continued to be less responsive to financial variables and closed the week down, influenced by news regarding the market fundamentals. Despite the relative recovery observed in some commodity markets over the past two weeks, current prices are still significantly levels seen one month ago. For further information, see [Commodity Observatory](#).

Japan: GDP growth and contributions (q/q % chg, s.a.)



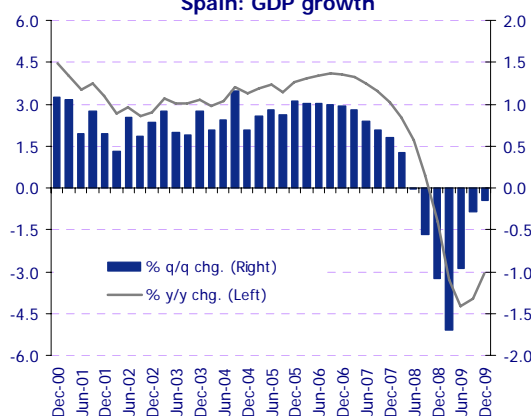
Source: BBVA-ERD

Peru: GDP (y/y % chg)



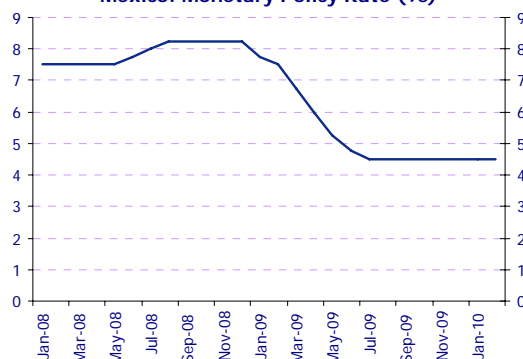
Source: INEI

Spain: GDP growth



Source: INE and BBVA ERD

Mexico: Monetary Policy Rate (%)



Source: Banxico and BBVA-ERD

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