

Global Weekly Flash

Uncertainty on the policy front in Europe likely to continue

The EU leader's dinner to prepare June 28 summit ended with no meaningful results, as expected. Plans to foster growth are mostly based on new European International Bank (EIB) capital but are unlikely to have any significant impact. Disagreements on Eurobonds and lack of discussion on a common deposit insurance scheme were apparent and will probably persist by the next summit on June 28-29, even if Europe seems to be ready to move to a "new stage" in the monetary union. In sum, there is no advance to reinforce financial stability in the eurozone to face an eventual accident following Greek elections on June 17.

- **Amid rising fears over a possible Greek exit from the eurozone, investors shy further away from risk**
 - As fears over the likelihood of a so-called "Grexit" mounted, investors' risk-off mood intensified this week. Weakness among EM currencies deepened, especially in Latam driven by large outflows. According to EPFR Global's data, for the week ending May 23, Latam-focused equity funds experienced a large outflow (-1.4% AUM, the largest since the first week of 2009). Besides, in another sign of increasing risk-aversion, EM dedicated bond funds saw outflows (\$478mn, equivalent to -0.34% AUM) for the first time in 19 weeks. A reversion of recent trends in risk and safe-haven assets seems quite unlikely considering that investors are likely to stay in a "risk-off" mode until they see breakthroughs in Europe's crisis resolution.
 - Elsewhere, the EURO-DOLLAR hit a 22-month low, dropping to 1.25. After showing resilience throughout the year, the euro has fallen 5% over the past three weeks, with weakness intensifying this past week as the crisis is worsening and there is a lack of policy response. Up until recently euro resilience seemed puzzling but was driven by the combination of a relatively stable interest rate differential and small capital outflows from the EZ over the past few months. However, as the fears finally take toll, there are reports that fund managers have been selling euro denominated assets this week after having tended to switch their holdings from peripheral to core countries.
 - Meanwhile, safe-haven rates continue to drop, especially German Bunds which fell to 1.35% this week. Investors' fears are such that the story that yields are telling us is that the return of principal rather than the return of capital is driving yields. As there is still no relief in sight for Europe, the probability of a continuing rally in safe-haven bonds is increasing even if Bund yields stand at record low levels and in spite of the significantly decrease already seen for 10y Treasury rates, interrupted only this week on the back of better-than-expected housing data and less-dovish-than-expected comments from Federal Reserve Bank of New York President William Dudley (expectations for U.S. economic growth, while "pretty disappointing" at around 2.4%, is sufficient to keep the Fed).
- **Weakness in economic data (unsurprisingly) points to further deterioration in Europe and increasing downside risks in China**
 - On the macro front, manufacturing confidence in the eurozone pointed to continued weakness. Euro flash PMIs and the German IFO Business Climate indicator fell sharply, the former pointing to further deterioration in activity, with all indices now in contraction. The EZ-Composite index fell deeper into contraction to 45.9 from 46.7 in April, with both the Services and Manufacturing indexes down to 46.5 and 45.0, respectively, and driven by sharper falls in Germany: the Composite index fell below the 50 mark, to 49.6 from 50.5. The IFO Business Climate indicator dropped to 106.9 from 109.9 in April (a minor drop to 109.4 was anticipated).
 - Elsewhere, the China flash PMI released by HSBC fell from 49.3 in April to 48.7 in May (staying below 50 for the seventh month in a row), suggesting that downside risks are increasing on deteriorating external conditions. In the US, manufacturing data this week also pointed to a loss of momentum in the near term. Markit, published a US flash PMI index for the first time. The headline estimate for May fell to 53.9 from 56.0 in April, and from an average of 54.6 in Q1 (the ISM averaged 53.3 in Q1 and stood at 54.8 in April). Besides, durable goods orders began the quarter in a soft note, as the Ex-Transportation index dropped -0.6% in April (vs +0.8% expected) dragged down by core capital goods' orders.

Next week: there are important events within the Europe. Ireland's referendum on the "Fiscal Compact" will take place on May 31. Recent opinion polls suggest Irish people is leaning to support the "Fiscal Compact". Besides, next week it is very relevant for Italian government's funding. Italy will sell EUR 11bn in bonds; and it faces bond redemptions for EUR12.8bn. On March 30, the European Commission will deliver their economic policy recommendations regarding the Six-Pack. Additionally, On the economic front, several important economic indicators will be released such as the US and Chinese PMI for May.

Calendar: Indicators

Eurozone: Flash HICP inflation (May, May 31st)

Forecast: 2.5% y/y	Consensus: 2.6% y/y	Previous: 2.6% y/y
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Headline inflation is expected to decline marginally in May to 2.5% y/y, driven by lower inflation in more volatile components, especially energy. In contrast, inflation of the rest of components are expected to remain broadly stable, resulting in an unchanged core inflation at 1.9% y/y. High oil prices combined with the continuous depreciation of the euro suggest that inflation should remain above the ECB target during 2012, although returning to the target at the end of the year. Core inflation is likely to remain hovering around 1.9% y/y in coming months to moderate timidly in H212. Upside risks continue to come from potential increases in oil prices, as well as potential tax hikes to meet fiscal targets, although recent soft data suggest that the depressed domestic demand could partly offset these effects.

Eurozone: Unemployment rate (April, June 1st)

Forecast: 11.0%	Consensus: 11.0%	Previous: 10.9%
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We expect the unemployment rate to have stepped up in April to 11%, from 10.9% in March, thus continuing the upward trend observed since mid-2011 and cumulating a 1.0pp increase since then. Given that the employment performance tends to follow activity fluctuations with a time lag of two to four quarters, and considering increasing fears about the intensification of the eurozone crisis, the unemployment rate is likely to increase slightly further along 2012. Confidence surveys for May also point in this direction, with firms' hiring intentions declining again but at a modest pace. PMI surveys by countries also show that divergences across countries should persist, with the largest increases in the unemployment rate to be recorded in countries with ongoing severe macroeconomic adjustments.

US: GDP (1Q12 second estimate, May 31st)

Forecast: 2.0%	Consensus: 1.8%	Previous: 2.2%
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The second estimate for first quarter GDP growth is expected to be slightly lower compared to the first estimate on account of weaker-than-expected data in March. In particular, the trade balance widened significantly despite accelerating export growth. Furthermore, the latest construction spending data noted a decline in public outlays for the fourth consecutive month, a component that will likely drag down government spending for 1Q12. Business inventories increased only slightly in March, although the total build for the quarter appears stronger than that in 4Q11. Consumption data arrived as expected at the end of the quarter and were likely already accounted for in the advance GDP figure.

US: Nonfarm Payrolls and Unemployment Rate (May, June 1st)

Forecast: 150K, 8.1%	Consensus: 150K, 8.1%	Previous: 115K, 8.1%
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Employment conditions weakened significantly throughout the past few months, with nonfarm payroll growth dropping well below the 200K level. Total payrolls in May are expected to increase at a slightly faster pace than in April but remain much lower than the stronger improvements seen in early 2012. Initial jobless claims have declined slightly since April but the monthly average is still higher compared to February and March. Regional manufacturing surveys continue to suggest strong employment gains despite mixed reports of slowing in overall activity. However, the sector's payrolls account for only a small portion of total employment growth. The declining participation rate, which in April reached a 30-year low, highlights the potential for an increase in the unemployment rate if individuals enter (or re-enter) the labor force.

China: PMI for (May, June 1st)

Forecast: 51.5	Consensus: n.a.	Previous: 53.3
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Weaker-than-expected activity outturns in April are causing the market to reassess expectations regarding the pace of China's growth. The official manufacturing PMI in May is thus expected to provide important signs regarding China's growth momentum. Thursday's flash estimate for private sector PMI (Markit) registered a slight downturn in May, to 48.7% from 49.1% the previous month, showing weak sentiment persists in the economy. Considering this flash outturn, as well as seasonal effects, we expect a decrease in the official PMI for May, however we expect it will remain above the +50 expansion/contraction threshold. That said, the government's recent comments emphasizing that it will help stabilize China's growth through further policy support, along with a stronger PMI outturn for May, could signal a rebound in growth momentum over the course of rest of this year.

Markets Data

			Close	Weekly change	Monthly change	Annual change	
Interest rates (changes in bps)	US	3-month Libor rate	0.47	0	0	21	
		2-yr yield	0.29	0	2	-19	
		10-yr yield	1.74	2	-24	-133	
	EMU	3-month Euribor rate	0.68	-1	-5	-76	
		2-yr yield	0.05	0	-7	-151	
		10-yr yield	1.37	-5	-37	-161	
	Exchange rates (changes in %)	Europe	Dollar-Euro	1.253	-1.9	-5.2	-12.5
			Pound-Euro	0.80	-1.0	-2.2	-7.8
			Swiss Franc-Euro	1.20	0.0	-0.1	-1.2
America		Argentina (peso-dollar)	4.47	0.2	1.3	9.4	
		Brazil (real-dollar)	2.00	-1.1	6.5	25.6	
		Colombia (peso-dollar)	1843	1.1	4.6	2.0	
		Chile (peso-dollar)	511	1.0	5.0	9.4	
		Mexico (peso-dollar)	14.01	1.4	6.4	20.7	
		Peru (Nuevo sol-dollar)	2.70	1.1	2.0	-2.0	
Asia		Japan (Yen-Dollar)	79.62	0.8	-2.1	-1.5	
		Korea (KRW-Dollar)	1185.43	1.1	3.9	9.5	
		Australia (AUD-Dollar)	0.978	-0.7	-5.6	-8.7	
Comm. (chg %)		Brent oil (\$/b)	106.8	-0.3	-10.3	-7.1	
		Gold (\$/ounce)	1567.8	-1.6	-4.6	2.0	
		Base metals	516.2	-1.1	-4.2	-14.9	
Stock markets (changes in %)	Euro	Ibex 35	6511	-0.8	-8.5	-36.5	
		EuroStoxx 50	2151	0.3	-7.4	-23.7	
	America	USA (S&P 500)	1321	2.0	-5.0	-0.8	
		Argentina (Merval)	2340	9.6	2.8	-28.3	
		Brazil (Bovespa)	54199	-0.6	-12.2	-15.7	
		Colombia (IGBC)	14494	0.7	-3.1	1.1	
		Chile (IGPA)	20494	-0.3	-6.1	-10.5	
		Mexico (CPI)	37495	1.7	-4.0	4.7	
		Peru (General Lima)	20706	1.0	-9.4	-7.5	
	Asia	Venezuela (IBC)	238634	-0.3	-7.5	198.0	
		Nikkei225	8580	-0.4	-10.3	-9.9	
		HSI	18713	-1.3	-9.4	-19.1	
Credit (changes in bps)	Ind.	Itraxx Main	175	-8	34	71	
		Itraxx Xover	720	-33	58	347	
		CDS Germany	99	-1	14	59	
	Sovereign risk	CDS Portugal	1218	-3	220	538	
		CDS Spain	541	-15	72	286	
		CDS USA	48	4	10	---	
		CDS Emerging	320	6	61	102	
		CDS Argentina	1256	71	286	641	
		CDS Brazil	159	4	34	51	
		CDS Colombia	149	4	35	44	
		CDS Chile	119	4	22	49	
		CDS Mexico	148	3	26	43	
		CDS Peru	161	4	34	34	

Source: Bloomberg and Datastream

Weekly Publications

Country	Date	Description
USA	05/24/2012	➤ U.S. Economic Watch. State Fiscal Stress Indexes 1Q12 Although revenue collection has improved and states have made substantial cuts to trim deficits, pressures persist as federal funding declines
	05/24/2012	➤ U.S. Economic Watch. State Activity Indexes April 2012 Regional MoM growth in the South and Southwest was robust in April, while other smaller and less populous states such as Maine, Alaska, and Wyoming slowed
	05/23/2012	➤ Banking Watch: Quarterly Credit Quality Update Total charge-offs have recovered more than 60% from the recession peak to nearly 1.2%, supporting improvements in overall asset quality Spanish version
	05/21/2012	U.S. Weekly Flash. Lower Energy Costs Limit Headline Inflation in April Headline consumer inflation was unchanged in April following three months of gains. The energy price index declined 1.7%, with gas prices down 2.6% after increasing 6.0% and 1.7% in February and March, respectively Chinese version Spanish version
EMU	05/24/2012	➤ Europe Flash: "Flash PMI disappoints also in May, with manufacturing pushing the index further down" Private sector activity deteriorated further in Eurozone, as reflected in flash PMI indices falling deeper in contractionary territory.
	05/23/2012	➤ Situación Europa. Segundo trimestre 2012 La economía de la zona euro se recuperará lentamente durante la segunda mitad del año. Las autoridades europeas deben clarificar el marco institucional y las políticas para los próximos años. <ul style="list-style-type: none"> • La economía de la zona euro se recuperará lentamente durante la segunda mitad del año. • La diferencia entre el centro de Europa y la periferia se explica por el estrés financiero y el importante ajuste fiscal en estos últimos. • Las autoridades europeas deben clarificar el marco institucional y las políticas para los próximos años. • Progresos hacia una unión fiscal, una estrategia de ajuste enfocada en el déficit estructural así como un mayor apoyo vía liquidez a los soberanos ayudarían a resolver la crisis
	05/21/2012	Europe Economic Watch: "Positive surprises in Q1-12, but the economic outlook remains gloomy". Economic confidence has improved in recent months, more than expected, but remains at very low levels
Spain	05/24/2012	➤ Spain Economic Outlook. Second Quarter 2012 <ul style="list-style-type: none"> • Recession confirmed, but no signs of further deterioration, while the on-going reforms will increase growth. • Global economic growth continues but uncertainty increases. • Europe, awaiting a credible agenda for growth and fiscal consolidation, becomes decoupled from global growth. • Spain: recession is confirmed, but not accelerating. • Current uncertainty is conditioning the short-term effect of reforms. • Building confidence depends on the design, execution, and communication of a credible set of reforms.
	05/24/2012	Flash España: "España: hipotecas sobre vivienda marzo 2012" Durante el mes de marzo se modera la caída de las hipotecas, una vez corregidas las variaciones estacionales
	05/21/2012	Situación Canarias. Primer semestre 2012 El turismo abre una ventana de oportunidad a la economía canaria. Acelerar la implantación de reformas, un reto ineludible al que se enfrenta la comunidad insular. <ul style="list-style-type: none"> • Continúa el crecimiento mundial pero se incrementa la incertidumbre. • Europa, a la espera de una agenda creíble de crecimiento y ajuste fiscal, se descuelga del crecimiento mundial. • España: se confirma la recesión pero no se acelera. • El turismo abre una ventana de oportunidad a la economía canaria. • Acelerar la implantación de reformas, un reto ineludible al que se enfrenta la comunidad insular. Presentación "Situación Canarias. Primer semestre 2012"

05/22/2012

Situación Uruguay Primer Semestre 2012

La actividad desacelera de manera suave, en sintonía con una menor demanda externa, dejando un crecimiento de 4,2% para 2012

- El crecimiento global se recuperará gradualmente, pero los riesgos están fuertemente sesgados a la baja
- Uruguay recupera el grado inversor por menor vulnerabilidad externa, potenciando crecimiento
- Leve deterioro del balance fiscal, reflejando el impacto del elevado precio de la energía y la desaceleración de la actividad, el superávit primario será de 1,4% del PIB
- Leve deterioro de la cuenta corriente por trabas y precios desfavorables, resultará en un déficit de 2% del PIB que será financiado por la inversión extranjera directa
- La fortaleza de los precios internos y la apreciación cambiaria condicionan al Banco Central de Uruguay, estimamos que la tasa de política monetaria se mantendrá en 8,75% hasta fin de año

Mexico

05/24/2012

Mexico Inflation Flash. May's first fortnight inflation: annual upturn caused by agricultural prices

General: Actual:-0.48% f/f vs. BBVA:-0.62% f/f Consensus:-0.45% f/f. Core: Actual: 0.14% f/f, vs. BBVA:0.03% f/f Consensus:0.11%

05/21/2012

Flash Bancario México. Captación bancaria: crece a tasa de dos dígitos

Captación a la vista: en marzo su crecimiento fue dinámico y de 15.7% nominal anual. Captación a plazo: su ritmo de crecimiento se ha moderado.

Asia

05/24/2012

Asia Daily Flash | 24 May 2012: China Flash PMI edges down; Gasoline price rises in India; Vietnam inflation slows to single digits

China's flash estimate of the private sector PMI (Markit) in May, released today, registered a slight downturn to 48.7% from 49.1% in April, mainly due to weakness in new orders

05/23/2012

Asia Daily Flash | 23 May 2012: China to increase SME financing options by allowing bond issuances; Japan leaves monetary policy unchanged; HKMA's rule change regarding RMB net open positions a long-term positive

The main news today was that China's authorities will allow SMEs to issue bonds through private placements starting next month, supporting SMEs seeking to broaden their sources of financing

05/22/2012

Asia Daily Flash | 22 May 2012: Japan's sovereign credit rating lowered by Fitch; RBI announces fresh measures to curb arbitrage as the INR's fall continues

The possibility that pro-growth measures will be on the table at tomorrow's EU summit lifted Asia's markets today, with the region's biggest gains coming from the Kospi (1.6%).

05/21/2012

Daily Flash | Asia | 21 May 2012: China's Premier calls for more fiscal measures to support growth; Thailand's Q1 GDP rebounds; Taiwan's export orders fall again

Statements from G8 leaders and China's Premier Wen Jiabao were enough to reverse the recent downtrend in Asian markets today.

Publications on May 25, 2012 to 11:00, Madrid time

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