Economic Research Department

Global

BBVA

Weekly Observatory

April 30, 2010

Financial markets: financial tensions increased early in the week but receded to end in a more positive mood

The week started with renewed tensions in debt markets, fuelled by new doubts surrounding Greece's rescue package, and particularly S&P downgrade of Greek debt to junk, and also of Spanish and Portuguese ratings. Markets reacted negatively with special focus on Portugal and Spain, whose spreads reached unprecedented levels. However, global markets closed the week in a more positive mood as a final deal over Greece is due to be reached in the next few days. Greek stock markets thus rebounded by 7%, Portugal's by 4.5% and Ireland by 3.5%. Also, their spreads to Germany's bonds also reduced significantly. Rating agencies are considered to have a key role in the sovereign crisis as their ratings normally determine the ECB's collateral rules. This week we also had a few bond auctions that were received with strong demand in Italy (bid-to-cover 1.8 for 10-year bond) and Germany. For further information, see Flow Watch.

EMU: 5-yr sovereign spreads against Germany

	CDS 29/04/2010	Cash 29/04/2010	Change in CDS Last week	Change in Cash Last week
Greece	671	852	55	115
Portugal	299	302	19	84
Ireland	194	113	10	8
Spain	170	112	-6	16
Italy	146	88	7	21
Belgium	83	74	4	11
Austria	73	42	1	6
France	65	14	1	0
Holland	42	10	2	-1
Finland	27	22	-2	3

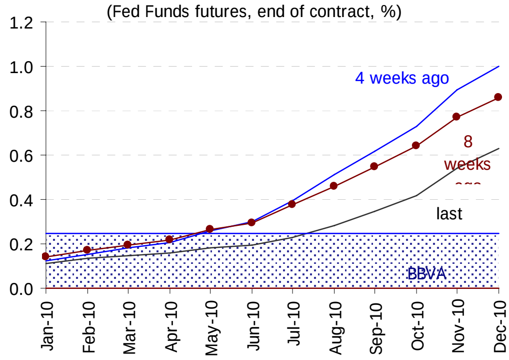
Source: Datastream and Bloomberg

US: the Federal Reserve maintained the target rate at 0-0.25%

Consumer confidence jumped in April, which could be a reaction to March's positive non-farm payroll report which shows that job market is improving. April's results are a positive sign for consumer spending because they indicate that the momentum experienced in 1Q10 could continue in 2Q10. The Fed also cited an improvement in household spending in Wednesday's FOMC Statement. While the Fed believes the economy is strengthening, it continues to expect inflation to remain subdued. As a result, it maintained the federal funds rate at 0-0.25%. In recent news, Obama nominated Ms Yellen as Vice-Chairman of the Fed, a move that is not expected to impact voting dynamics. For further information, see US Weekly Observatory.

US: Fed Funds Expectations

(Fed Funds futures, end of contract, %)



Eurozone: announcements expected for this weekend on Greece; positive data on the week

This weekend will be key for the Greek crisis, as the EU is bound to announce a large rescue package for three years (rumors to up to 120 bn euro and beyond), while the Greek government will announce its consolidation plan negotiated with the IMF and EU institutions, which has been leaked and is also larger than previous plans. On the data front, quarterly sector accounts revealed that the household savings rate continued falling in Q4 in the Eurozone, though marginally, while the unemployment rate stabilized at 10% in March, with a surprising fall in Germany and increases in Italy and Spain. The EC sentiment survey for April was in line with PMI's published last week, signaling a significant improvement in confidence. Inflation accelerated by 0.1pp to 1.5% in April, according to the flash, probably driven by higher energy prices, while core inflation should have decelerated somewhat further. On the ECB front, no relevant changes are expected for next week's meeting, while the press conference is expected to deal again with the Greek crisis. For further information, see Europe Weekly Observatory.

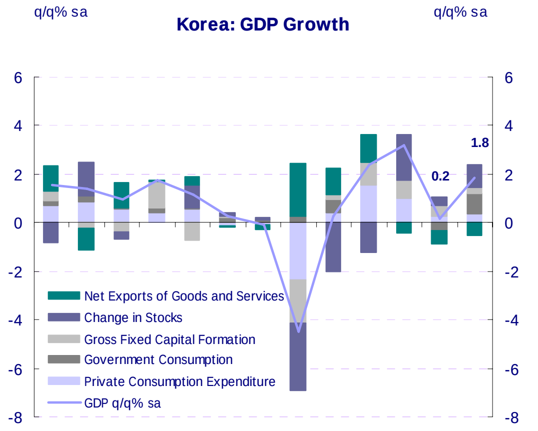
Unemployment rate (as % active population)

	Mar-09	Jan-10	Feb-10	Mar-10
Euro zone	9.1	9.9	10.0	10.0
Germany	7.4	7.4	7.4	7.3
France	9.1	10.0	10.1	10.1
Italy	7.8	8.5	8.6	8.8
Spain	17.4	18.9	19.0	19.1
Portugal	9.0	10.3	10.3	10.5

Source: Eurostat

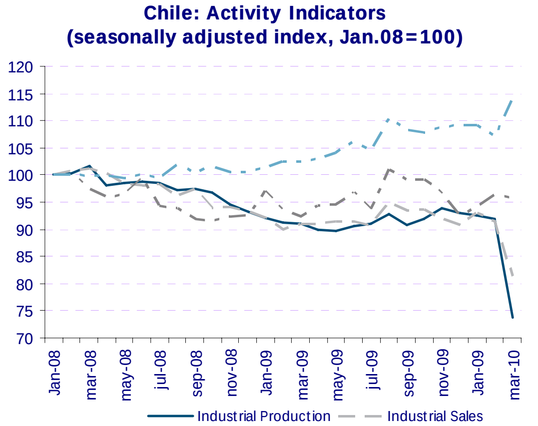
Asia: new strong indicators can not deal with Europe turbulences

Fresh indicators of strong growth momentum failed to stem spillovers from the Greek debt crisis and European ratings downgrades on regional financial markets. Strong losses were recorded in China, Hong Kong and Australia. Meanwhile, Asian currencies for the most part remained stable. Korea's 1Q10 GDP expanded above market expectations driven by strengthening domestic demand. A higher inflation in Australia, although still within the 2-3% target range, sparked expectations of further monetary tightening. As expected, the Bank of Japan left its reference rate unchanged. This coming week, markets will focus on monetary policy decisions in Australia and Indonesia, and inflation readings in Korea, Indonesia, Thailand and the Philippines. For further information, see [Asia Weekly Observatory](#).



Latin America: strength in FX markets despite rising risk aversion

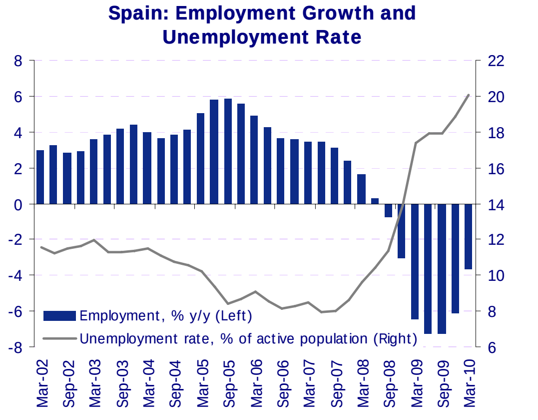
Latin American currencies displayed signs of strength this week despite an increase in both global risk aversion and regional spreads. The performance follows at some extent the positive flow of indicators released throughout the week. In Chile the retail sector expanded, providing support to a positive performance of the GDP in spite of a sharp decline in the industrial activity (which is a consequence of the earthquake). Positive news regarding the resolution of Argentinean holdouts and also regarding the improvement of credit conditions in Colombia and in Brazil. In the latter, the Central Bank started this week to adjust interest rates upwards as expected. For the next week we highlight the release of inflation figures in Peru, Colombia and Brazil. In addition the Central Bank of Peru will meet to decide on interest rates. For further information, see [Latin America Weekly Observatory](#).



Source: INE and BBVA

Spain: the Unemployment rate rose to 20% in 1Q10

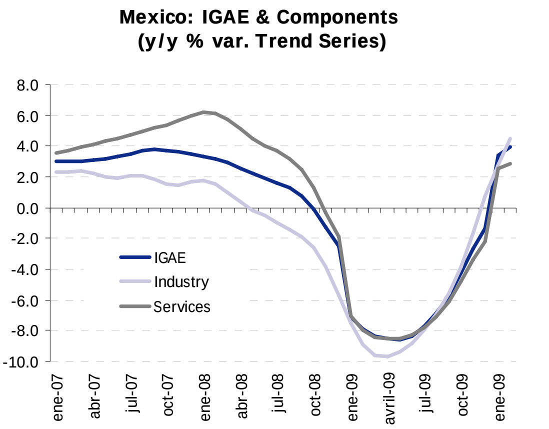
The most important economic news in Spain this week was the release of the Labor Force Survey for 1Q10. Total employment fell by 252.000 people in 1Q10 (514.000 fewer than in 1Q09), while the number of unemployed rose by 286.000 people (803.000 during 1Q09). Overall, the unemployment rate rose to 20.1% from 18.8% in the previous quarter. This week's data also brought the European Commission confidence indicators which have showed an increase in both Consumer and Industrial confidence in April for Spain (2.2 and 3.3 points, respectively). On the other hand, retail sales rose by 3.5% y/y (1.1% m/m swda) in March, showing a better than expected performance. Finally, the HCPI flash suggests that headline inflation may have risen by 0.1 pp to 1.6% y/y in April. Next week's data will include: Social Security affiliation and registered unemployment for April, as well as the Industrial Production Index for March (Prior: -1.9% y/y wda).



Source: INE and BBVA ERD

Mexico: Banxico, upward revision in 2010 growth and unchanged inflation perspective

February's IGAE surprised positively (0.5% m/m vs. -0.3 m/m estimated) due to highly volatile agriculture sector. Industry is recovering but at a slower pace than in 4Q09, expanding 0.6% m/m (4.4% y/y). Manufacturing activities with tight links with the US cycle are still leading the Mexican recovery. Domestic expenditure expected improvement should help to services sector speed it up. Banxico's inflation report as of 1Q10 improves its forecasted growth from a 3.2-4.2% range to a 4-5% range. In addition, the central bank maintains its inflation path for 2010-11, in a 4.75-5.25% range in 4Q10 and convergence to its inflation objectives since 1Q11. The report also mentioned the economic slack as a key element in monetary terms. Next week we will have a first clue on 2Q10 indicators through April's Consumer and Manufacturing Indicators and inflation figures. For further information, see [Mexico Weekly Observatory](#) (in Spanish).



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