As at January 22nd, 2012

Greece Private Sector Involvment Negotiations Continue

United States

Better Investors' Sentiment

We started the year with concerns about Chinese growth, European sovereign and bank recapitalization risks and questions over the sustainability of US economic growth. Those fears seem to be fading so far in 2012 as balances on deposits with the ECB dropped sharply this week and US jobless claims fell to their lowest level since March 2008. The ECB continued supporting Portuguese bonds and Spain has completed 19% of their funding needs for 2012

The major news that the IMF will attempt to increase its lending capacity by $500 billion eased investors' fears. Consequently, markets responded favorably despite the US Treasury denying any intention to seek additional resources for the IMF and the Bundesbank head Weidmann mentioning that he sees exceptional risks to the Euro zone economic outlook and reiterated his opposition to the ECB unlimited bond buying.

The main driver for markets in shaping sentiment remains the Greek debt Private Sector Involvement negotiations, which seem to be centered around a proposal that would see a haircut of around 68%, but the level of holdouts remains a big sticking point. As a result, Greek PM Papademos continues to threaten the use of legislation to force acceptance if necessary.

Last but not least, rating agencies continued their assault on the European zone on Thursday with Moody's affirming that global bank ratings are likely to be lowered this year and contended that most European banks are vulnerable to the Euro area debt crisis. Moody's anticipates they will put the ratings of several of these banks under downgrade review in Q1 of 2012.

On the foreign exchange side, the Euro broke the short-term downtrend and took out a number of stop losses. After hitting a new low of 1.2626 at the beginning of the week, the Euro moved sharply higher to end of the week at 1.2930.

Despite the UK Nationwide's consumer confidence index dropping in December, and the Guardian newspaper reporting the UK's national debt level to 500% of GDP, the Sterling Pound followed the Euro's movement and positive market sentiment to close the week at 1.5576.

US Job Continue to Impress despite Volatile January Data

In the largest one-week decline since the week of 24 September 2005, applications for unemployment insurance payments plunged by 50,000 to 352,000 in the week ended January 14, less by 30k than economists had forecasted. The Labor Department relies on reports from state agencies, and because many field offices were shut down on Monday, Thursday's report represents an estimate. January is also known as a particularly volatile month. The previous week's figure was revised up to 402,000 from 399,000.

US Inflation as Expected, However Mixed Signals from the Housing Sector

US Consumer Price Index came flat again in December, leaving the y/y headline inflation at 3.0%, down from 3.9% in September. As expected, the core CPI excluding food and energy posted a 0.1% m/m increase in December, although remained flat compared to November. According to the Fed, inflation is likely to remain around this level until the second quarter before gradually declining through the year.

On the other hand, December's housing starts dropped more than expected, declining 4.10 m/m to a 657k pace. Last month's decline was driven by a 20.4% drop in construction of multifamily homes with at least two units, a volatile part of the market. However, construction of single-family homes, which made up about 72% of housing starts, rose by 4.4%. The data also showed newly issued building permits fell 0.1% in December from a month earlier to an annual rate of 679,000. Those results were in line with expectations.

The Empire State Manufacturing Expands in January

The Empire State Manufacturing Survey indicated an expansion at the fastest rate in nine months in January. The general business conditions index climbed 13.5 points from a revised 8.2 in December compared to expectations of 11. The index has been in a strong upward trend after remaining stuck below zero from June through October.

New Orders Index rose eight points to 13.7 and the shipments index inched up to 21.7. Employment indexes were positive and higher, pointing to higher employment levels and a longer average workweek. Future indexes conveyed a high degree of optimism about the six-month outlook, with the future general business conditions index rising nine points to 54.9, its highest level since January 2011.

Europe & UK

Greece PSI Negotiations Continue

Greece and its private bondholders continued negotiation last week in an attempt to reach a vital debt swap deal to avoid a messy default by Athens. European leaders also agreed to keep the combined ESM/EFSF capacity at 500 billion Euros, but will review it in March and may raise it by the permanent fund's board of governors once it is operational, according to a draft treaty.
Finally, the ESM treaty will aim to create an incentive for the passage of the 'fiscal compact'. Only countries that have started ratification of the compact will have access to the ESM.
In parallel, the International Monetary Fund announced Wednesday that it was seeking as much as $500 billion more to lend as it prepared to slash its forecasts of global growth.
The fund estimated that the world would need $1 trillion in the coming years for loans to countries with short-term difficulties paying their bills or because of concerns about prospective trouble in the volatile bond markets. Given that the fund has unused lending capacity of about $380 billion, it said it would seek to raise as much as $500 billion in new money to lend, plus $100 billion as a cash buffer. The new money includes $200 billion that European Union countries committed in December.
In meetings of the fund's executive board this week, many participants "stressed the necessity and urgency of collective efforts to contain the debt crisis in the euro area and protect economies around the world from spillovers.

Fitch Ratings Agency take on Greece

A Fitch Ratings director said Greece will soon default on its massive debt, according to a report by Reuters Tuesday. The news agency quoted Edward Parker, managing director for Fitch's as saying "it will happen," but the default will not be disorderly as some have feared. The big risk, the analyst added, is that of a "disorderly" default by Greece, one that could rock markets around the world and create tougher credit conditions for other countries trying to roll over existing debt.

Sarkozy Dismisses France's AAA Credit Downgrade

In response to the recent downgrade of France's AAA credit rating, French President Nicolas Sarkozy attacked rating agencies this week by mentioning they do not set the economic policy of France and urged instead a focus on boosting growth and competitiveness to bring Europe out of the crisis. At a press conference following a Madrid meeting with Spanish Prime Minister Mariano Rajoy, Sarkozy said "We must respond with calm and put it into perspective. In my view, these decisions do not change anything. We have to reduce spending and improve competitiveness". Sarkozy also pointed out that while France was downgraded by one agency on Friday, another agency confirmed on Monday that France will retain its triple-A rating.

German ZEW Shows the Largest Increase Since 1991

German ZEW index showed the biggest jump ever in January. The index rose to -21.6 from -53.8 in December, the largest single monthly increase since the survey started in 1991. The data suggests that the German economic activity was likely to "stabilize further instead of deteriorating further".

Decent UK Retail Sales

UK retail sales volume rose in December, despite the slowing economy, boosted by record sales of clothing and footwear. The volume of retail sales including automotive fuel rose 0.6% from November and was 2.6% higher than in December last year. Sales in December showed a significant rebound from the previous month's figures when sales fell a downwardly revised 0.5% on the month and increased a downwardly revised 0.4% on the year.
Economists were expecting sales to rise 0.7% on the month, and be 2.4% higher than in December last year.

The volume of retail sales in the fourth quarter was 1.1% higher than in the third, the strongest quarter-on-quarter growth since August 2010.

Asia

Japanese Manufacturers Remain Weak

Reuters Tankan survey for January showed sentiment amongst Japanese manufacturers remaining weak, undermined by worries over the Yen's gains and a global slowdown. The manufacturers sentiment index, derived by subtracting the percentage of pessimistic responses from optimistic ones, stood at - 5, meaning pessimists outnumber optimists, the Reuters Tankan showed. It was unchanged from December, marking the second straight month of negative readings, though it stopped worsening for the first time in four months.
The index for non-manufacturers on the other hand held steady at + 6, and is expected to improve to + 10 in April. That would be the highest reading since December 2007, led by gains in sectors including real estate, construction, and retail/wholesale.

China's Growth Slowing

China real growth in GDP slowed further to 8.9% Y/Y in Q4 from 9.1% Y/Y in Q3, but stronger than market expectations of 8.7% Y/Y. A 2.0% Q/Q expansion shows the economy growth is stabilizing. China's economy expanded 9.2% Y/Y in 2011 in line with market consensus, compared to a 9.4% Y/Y gain in 2010.
Both industrial production and retail sales posted faster-than-expected growth last month due to relatively strong holiday demand. There was some external liquidity drained from China's banking system last month as outstanding FX purchases declined for the third consecutive months in December. However, the PBoC injected RMB 169 billion liquidity into the banking system at the beginning of the week.

Commodities

Iran Confronts Saudi Arabia against Increasing Oil Production

Crude Oil remains at the mercy of political events driven by the latest development in the Middle East. Iran issued a direct warning to Saudi Arabia against increasing its production of oil to compensate for any drop in Iranian exports due to sanctions. Iran's Foreign Minister, Ali Akbar Salehi said "We invite Saudi officials to further reflect on and consider" their pledge to make up for any cut in oil exports adding such a move "will create all possible problems later" and are "not friendly signals".

Gold Positive at the beginning of the year

Gold prices rose this week, in tandem with the general risk appetite, and with political tensions rising in the Middle East. Additionally, the weakening Chinese growth fuelled investor hopes for monetary stimulus from China trying to boost productivity through monetary easing.
On physical demand, India hiked its gold import duty by 90% and doubled its silver tax this week as the world's biggest consumer of gold sought to increase revenues.

Kuwaiti Dinar at 0.27835

The USDKWD opened at 0.27835 on Sunday morning.

Rates – 22 January 2012

	Previous Week Levels				This Week's Expected Range		3-Month
Currencies	Open	Low	High	Close	Minimum	Maximum	Forward
EUR	1.2680	1.2626	1.2986	1.2931	1.2855	1.3000	1.2920
GBP	1.5318	1.5273	1.5579	1.5576	1.5420	1.5670	1.5550
JPY	76.97	76.55	77.32	77.01	76.10	77.60	76.80
CHF	.9524	.9307	.9307	.9345	.9250	.9400	.9315