

MARKET REPORT

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Rising bond yields in France

Moody's warns that the negative growth prospects and rising debt yields in France might have a negative effect on their credit rating, but they added that the grade itself is not under pressure "at this stage".

Spanish election, credit rating and economic outlook

In Spain, the bond yields are rising despite the election results where the right-wing Popular Party won with a majority of 186 seats in the 350-seat parliament. Spain currently has an AA-credit rating and although its outlook remains negative, S&P assured that that rating is not to be changed. The majority could allow reform in Spain to take place soon but S&P says that "Spain must grapple with weak growth prospects, rigid labor markets and high debt". Those are the main reasons why the average yields on the country's short-term debt hit 14-year highs this week.

Eurozone rescue fund fiasco

As we wrote in the last Market Report, the Eurozone rescue fund is looking severely wounded and EU has now mentioned their new solution; a proposal for the joint issuance of bonds among member nations. The deteriorations in market conditions and surging bond yields, the Eurozone may not be able to reach its goal of leveraging up its €440B EFSF rescue fund to over €1T and it is expected to fall well short of its billing.

Disastrous bond auctions in Germany and Italy

An auction of €6B German 10-year bonds attracted bids of only €3.644B this week, this was the worst demand on record concerning government bonds in Germany. It is a major hit for the trust of Germany as there are increasing worries over the cost they may have to cover because of the crisis.

Italian yields also soared after another horrific EU bond auction, their yields almost doubled to an average of 6.5% as Italy sold €8B of short term bonds in an auction this week. Even

ECB buying has not been able to slow down the increase in yield.

Japan, bond issuance and deflation

Japan will issue new bonds to pay for the earthquake reconstruction and help fight the strong yen. Their exports fell by 3.7% in October and their trade deficit is currently at \$3.56B. They are also stuck in deflation as their core CPI dropped a monthly 0.1%

Harsh words from China

The Chinese Vice-Premier Wang Qishan said that "An unbalanced recovery would be better than a balanced recession". In other words, China should focus on its own growth rather than the trade surplus with the U.S. China might not be there to have our backs as we dearly hope.

Payroll tax cuts and stress tests in America

President Obama is trying to get Congress to preserve an expiring payroll tax cut, to agree to this, the republicans will probably want additional spending reductions to offset the \$168B cost. The Fed has also introduced new bank stress tests where banks have to model a severe Eurozone recession with a 6.9% real GDP decline. The six largest U.S. banks will also need to estimate losses if a crisis like the one in late autumn 2008 appear again.

OPEC production quotas and possible European embargo of Iranian oil

Senior Saudi Arabian and Iraqi oil officials as well as OPEC's secretary general said that that want the organization to maintain current production quotas as prices have remained high. OPEC has previously mentioned that some members may cut output. France also wants to boycott Iranian oil with an European embargo to keep prices above \$100 a barrel despite slowing economic growth. The U.K. broadly support this but there is strong resistance from Italy and Spain that heavily rely on Iranian oil.

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