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## WEEKLY MARKETS COMMENT



Eurozone finance ministers agreed to a second official programme for Greece of up to €130bn until 2014, and finalised measures to reduce the Greek public sector debt burden to 120.5% of GDP by 2020. On the Private Sector Involvement (PSI) to be launched on Wednesday, private sector Greek bondholders will be asked to take a loss of 53.5% on the nominal value of their bonds instead of the previously agreed 50% write-down. The Greek government will submit to the Greek parliament a draft bill which, if passed, will introduce a collective action clause into eligible Greek-law governed bonds of the Hellenic Republic, effectively enforcing losses through retroactive CACs on bondholders who will not take part in the debt swap.

The Official Sector Involvement (OSI) has two main elements: 1) interest rates on loans to Greece's first programme will be reduced retroactively, implying a lower margin of 150bp, delivering a reduction in the Greek debt burden worth 2.8ppt by 2020. This will be funded by the profits generated by the ECB from its SMP holdings, which will then be passed on to NCBs and ultimately to their own governments that provided the bilateral funding to Greece under the first programme. 2) National central banks who hold Greek bonds in their investment portfolios will pass on to Greece an amount equal to any future income arising from these holdings - delivering a further 1.8ppt reduction in debt to GDP by 2020.

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To ensure thorough implementation, two "*prior actions*" have been agreed: 1) the Eurogroup deemed it essential to further strengthen Greece's institutional capacity by bolstering its Task Force for Greece with an enhanced and permanent presence to provide and coordinate technical assistance; and 2) the Eurogroup welcomes the intention of the Greek authorities to pay an amount corresponding to the coming quarter's debt service directly into a segregated account of Greece's paying agent, and the intention to introduce over the next two months in the Greek legal framework a provision ensuring that priority is given to debt servicing payments.

The Eurogroup introduced additional conditionality by stipulating that the official sector will decide on the precise amount of financial assistance once the results of the PSI are known and prior actions have been implemented.

In China the People's Bank of China (PBOC) announced it will cut the Reserve Requirement Ratio (RRR) by 50bps, effective Feb. 24. This will bring the RRR to 20.5% for large banks and 18.5% for small and medium-sized banks. This is the first cut in 2012 and the second cut since Nov 2011. This move will likely inject Rmb390bn into the banking system.

This much later-than-expected cut is in line with Citi Analyst's view that the downturn of the Chinese economy wouldn't be altered without further policy easing, and that Chinese authorities are still keen to achieve GDP growth above 8% in 2012. The PBOC has been lagging behind the curve and may have to catch up with more easing to repair already damaged credit demand. We believe that three or more RRR cuts are needed this year to restore the confidence of business leaders in order to promote more investment in the near-term. The LTRO in Europe and possible QE3 in the US may weigh on the degree of further easing, but for now, concerns about a growth downturn are likely to outpace inflation worries.

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