GLOBAL MARKETS ANALYSIS
Monetary and Capital Markets

Global Markets Monitor

FRIDAY, JANUARY 31, 2020

- **French and Italian economies unexpectedly shrank in Q4** (link)
- **WHO declares international emergency, does not call for trade or travel bans** (link)
- **US 3m-10y yield curve inverts intra-day on virus concerns** (link)
- **More holiday extensions in Chinese provinces set to weigh on Q1 growth** (link)
- **New data shows growing concentration of US equity ownership** (link)

US | Europe | Other Mature | Emerging Markets | Market Tables

Virus, growth anxieties weigh on markets

Disappointing economic data add to the list of downside risks weighing on financial markets this morning. Equities are continuing to slump on virus concerns, weak euro area growth numbers, and earnings reports showing a dimming capex outlook. Markets were briefly buoyed yesterday when the WHO's announcement of an international emergency did not include a call for further restrictions on trade or travel. These gains have been largely unwound however as the US upgraded its warning against travel to China, confirmed coronavirus cases jumped to near 10,000, and euro area data surprised to the downside. Notably, the 3-month/10-year yield curve – historically an indicator of a coming recession – is once again in negative territory, for the first time since last October. Looking ahead to next week, markets may continue to see volatility as Chinese onshore markets re-open after an extended holiday. Currently, offshore futures markets are pricing a roughly 7 percentage point drop for onshore Chinese equities.

Key Global Financial Indicators

Last updated: 1/31/20 8:13 AM	Level: Last 12m	Level: Latest	Change from Market Close: 1 Day	7 Days	30 Days	12 M	YTD
Equities					%		%
S&P 500		3284	0.3	-1	2	21	2
Eurostoxx 50		3674	-0.5	-3	-2	16	-2
Nikkei 225		23205	1.0	-3	-2	12	-2
MSCI EM		43	-0.2	-4	-4	0	-4
Yields and Spreads					bps		
US 10y Yield		1.55	0.2	-13	-36	-108	-36
Germany 10y Yield		-0.42	-1.1	-8	-23	-57	-23
EMBIG Sovereign Spread		312	1	5	19	-54	19
FX / Commodities / Volatility					%		
EM FX vs. USD, (+) = appreciation		59.9	-0.3	-1	-2	-7	-2
Dollar index, (+) = $ appreciation		97.8	-0.1	0	1	2	1
Brent Crude Oil ($/barrel)		58.5	0.4	-4	-11	-5	-11
VIX Index (%, change in pp)		16.9	1.4	2	3	0	3

Colors denote tightening/easing financial conditions for observations greater than ±1.5 standard deviations. Data source: Bloomberg.

United States

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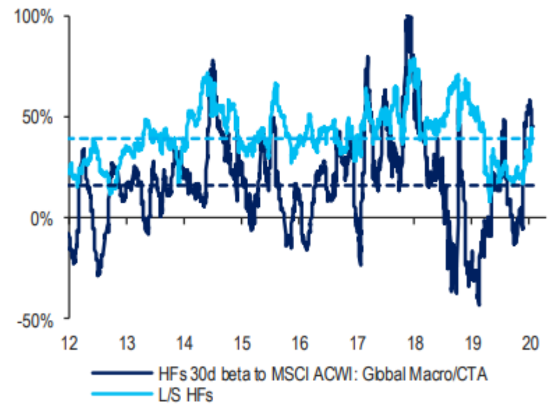
Stocks pared losses after WHO declared the virus outbreak an international emergency without recommending travel or trade restrictions. US indices rebounded from a near 1% loss to close modestly higher. Treasury yields gave unwound large intra-day declines to close just 2 bps lower. Earlier in the session, the yield curve dropped 5 bps across the curve, with 3-month-10-year slope dipping below zero for the first time since October, as investors ramped up bets of easing following today's anemic PCE number.

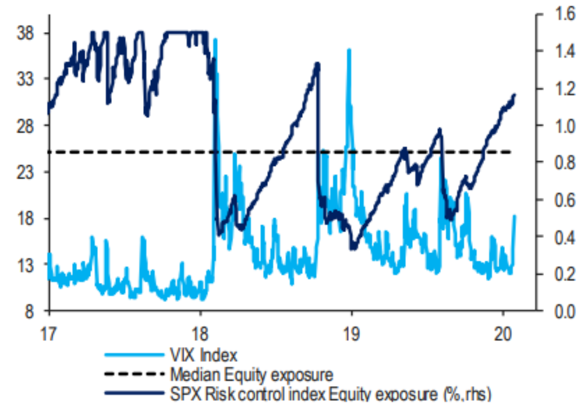
"Fast money" investors have substantially increased their equity exposures. Hedge funds and other systematic funds appear to have increased their exposures to equities significantly in recent months, which may have helped drive the equity rally that began in Q4 of last year. Analysts warned that the unwinding of these elevated positions could exacerbate market reaction to negative headlines.

Equity exposure of HFs – Macro, CTAs & L/S has increased significantly



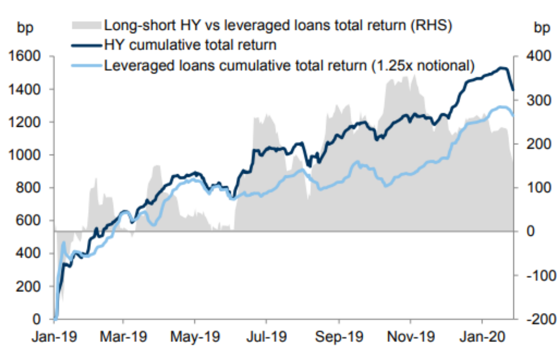
Source: HFRX, Datastream

As volatility went back to prior lows, leveraged funds materially increased equity exposure in Q4

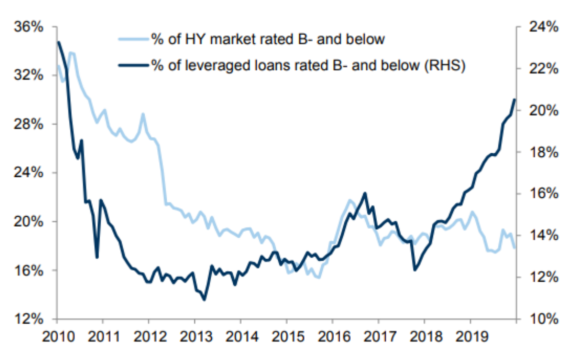


Source: Bloomberg

Leveraged loans have outperformed high yield bonds in January. The relative strength is driven in part by a modest improvement in flows as loan funds received $688 mn cumulative net inflows, as well as by higher risk appetite following the underperformance in 2019H2. However, analysts believe the recent strength will be temporary, given the still challenging fundamentals (significant uptick in downgrades in the lower-rated credits), concentrated ownership in the secondary market, and a less favorable valuation following the recent wave of downward re-pricing activities (see Tuesday's GMM).



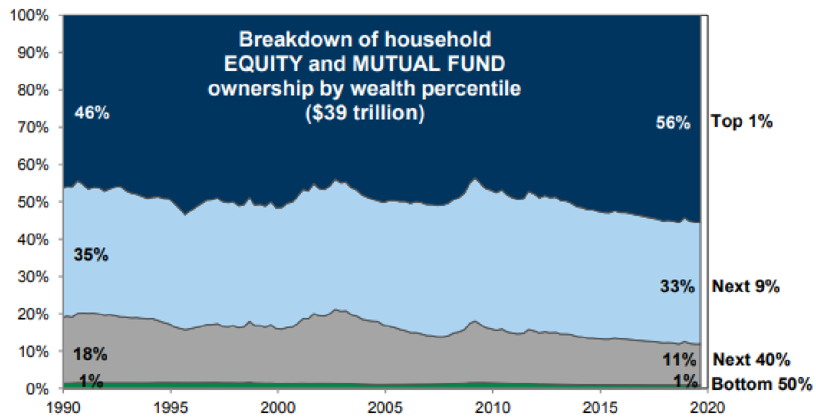
Source: S&P Capital IQ LCD, ICE-BAML, Goldman Sachs Global Investment Research



Source: S&P Capital IQ LCD, iBoxx, Goldman Sachs Global Investment Research

Concentration of household equity ownership is at record high, according to Goldman research based on the newly published Distributional Financial Accounts. US households owns 36% of US equities, of which 56% is owned by the top 1% households by wealth, and only 12% is owned by the bottom 90%. The gap between these two groups is at a record high. Over the past 30 years, the top 1% household were the sole net buyer of equities at $1.2 tn, compared with the $1 tn net selling from the remaining 99%. Moreover, the equity allocation of the top 1% households has risen near its all-time high to 61% of total assets. Any shift in their asset allocation will have a significant impact on the markets. While private funds are included in households, Goldman estimated that they account for only 10% of aggregate household holdings.

Exhibit 2: The top 1% holds 56% of all household equities (corporate, noncorporate, and mutual funds)
as of 3Q 2019



Source: Federal Reserve Board, Goldman Sachs Global Investment Research

Exhibit 5: The top 1% accounts for the majority of positive equity and mutual fund demand from households
flows as of 3Q 2019; net worth estimates as of 2016

Household wealth percentile	Net worth of avg. household ('000s)	Estimated equity and mutual fund demand ($ billions)							
		2015	2016	2017	2018	2019 Ann.	Total: Last 5 yrs	Total: Last 10 yrs	Total: Since 1990
Top 1%	$22,733	($52)	$150	$546	($329)	$533	$848	$1,778	**$1,215**
Next 9%	3,049	61	(47)	(48)	18	(37)	(51)	(169)	**(356)**
Next 40%	516	(38)	(65)	6	10	(21)	(109)	(124)	**(615)**
Bottom 50%	18	(9)	0	15	(11)	17	13	17	**(36)**
All households	**$717**	**($37)**	**$39**	**$519**	**($312)**	**$492**	**$700**	**$1,502**	**$208**

Source: Federal Reserve Board, Goldman Sachs Global Investment Research

Europe

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Euro Area

Equities (-0.5%) fell as euro area growth slowed to 0.1% qoq (0.2% expected) or 1.0% yoy (1.1% expected) in 2019Q4.

The French economy unexpectedly contracted 0.1% qoq (in contrast to growth of +0.2% qoq expected) and **the Italian economy shrank 0.3% qoq** (+0.1% expected).

Euro area core inflation also disappointed at 1.1% in January (+1.2% expected, from 1.3%). As expected, headline inflation in the euro area rose to 1.4% yoy in January (rom 1.3% in December). The euro was little changed at $1.10.

German and French 10-yr bond yields fell 1-2 bps (with U.S. 10-yr yields 3 bps lower at 1.56%). Italian 10-yr spread to bunds are little changed at 135 bps.

Shares of Banco Sabadell (a medium-sized Spanish bank focused on unsecured, consumer & SME, lending) **are trading 11% lower** after the bank increased its credit costs +60% qoq in 2019Q4 and guided for even higher credit costs in 2020. Contacts argue that the rise in credit costs is far from an idiosyncratic issue, as other local players have reported higher than expected credit costs in 4Q19 (Bankia) or are flagging the risk of higher provisions to come (Bankinter, CaixaBank). **European bank equities are down 5% ytd (1% today).**

United Kingdom

The markets are pricing in a 60% probability of BoE rate cut but a more aggressive easing cycle has been priced out since yesterday's BoE meeting. The British pound gained 0.3% on improving data releases such as U.K. consumer confidence in January and mortgage approvals in December.

Other Mature Markets back to top

Japan

The yen held steady while equities pared earlier gains to end the day modestly higher. The Topix rose 0.6% on the day, insufficient to erase losses sustained over the week. **Longer-dated JGB yields rose** following the BoJ's announcement that it will buy fewer super-long bonds. The frequency of monthly purchases for bonds maturing in 10-25 years and over 25 years will be lowered from three times to two. At the same time, the BoJ raised the indicative buying range for each operation in the 10-25 year maturity range by ¥50 bn ($459 mn), which would only partially offset the reduced frequency of purchases. The 30-year bond rose 2 bps to 0.35% while the 2-year yield fell 1 bp to -0.17%.

Emerging Markets back to top

Asian equities were mixed, erasing earlier gains to end the week on a somewhat positive note. Korean bourses underperformed (-1.4%) while others posted modest gains. **In currencies, the Korean won underperformed** (-0.6%), suffering its biggest weekly depreciation (-2.0%) since last May amid concerns that the spread of coronavirus will weigh on the Korean economy. Notably, according to news reports, Hyundai Motor canceled overtime duty at all South Korean plants as two Chinese suppliers of wire rings suspended operations on coronavirus concerns. **EMEA stocks were also mixed**, with losses in Poland (-0.9%), South Africa (-0.9%), and UAE (-0.5%); and gains in Egypt (+1.1%), Romania (+0.7%), and Saudi Arabia (+0.7%). Currencies were mostly stable. **Latin American assets experienced broad-based losses yesterday** as the WHO declared the coronavirus to be an international emergency. Mexican (-0.5%) and Chilean (-0.5%) equities saw the biggest losses. Among regional currencies, the Colombian peso (-0.8%) depreciated the most against the dollar as oil prices dropped, followed by the Chilean peso (-0.6%) and the Brazilian real (-0.5%). MSCI EM stocks dropped by 2.3%, the biggest daily decline since August last year.

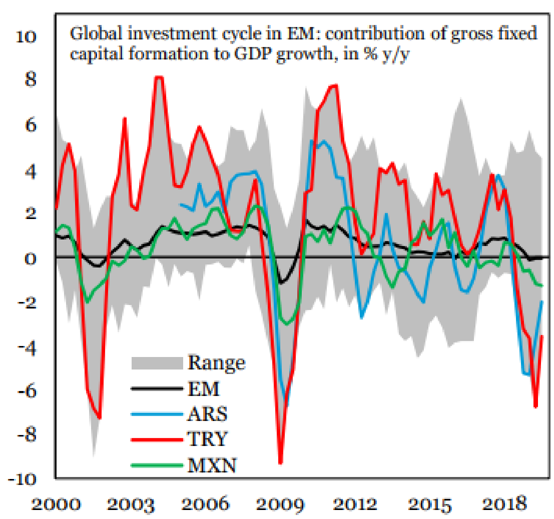
Key Emerging Market Financial Indicators

Last updated: 1/31/20 8:10 AM	Level: Last 12m	Level: index	Change: 1 Day	Change: 7 Days	Change: 30 Days	Change: 12 M	YTD
Major EM Benchmarks			%				%
MSCI EM Equities		42.98	-0.2	-4	-4	0	-4
MSCI Frontier Equities		30.74	0.2	-2	1	9	1
EMBIG Sovereign Spread (in bps)		312	1	5	19	-54	19
EM FX vs. USD		59.90	-0.3	-1	-2	-7	-2
Major EM FX vs. USD			%, (+) = EM currency appreciation				
China Renminbi		6.94	-0.5	-1	1	-2	0
Indonesian Rupiah		13655	0.0	-1	2	2	2
Indian Rupee		71.35	0.2	0	0	0	0
Argentine Peso		60.24	0.0	0	-1	-38	-1
Brazil Real		4.27	-0.5	-2	-6	-15	-6
Mexican Peso		18.84	-0.3	0	0	1	0
Russian Ruble		63.63	-0.6	-2	-3	3	-3
South African Rand		14.93	-1.1	-4	-6	-11	-6
Turkish Lira		5.98	-0.2	-1	-1	-14	-1
EM FX volatility		6.70	0.0	0.6	0.1	-2.2	0.1

Colors denote tightening/easing financial conditions for observations greater than ±1.5 standard deviations. Data source: Bloomberg.

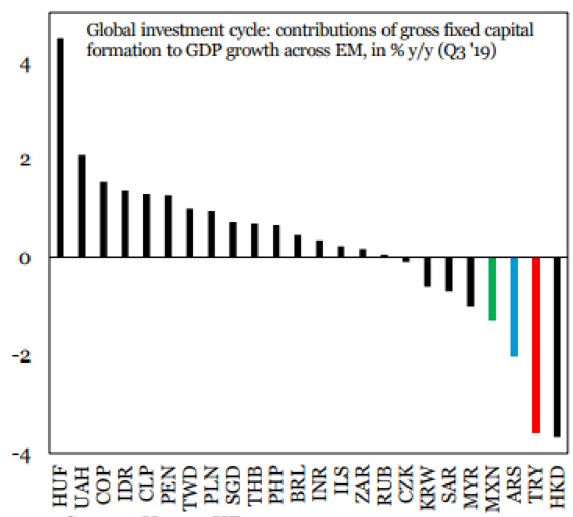
Many emerging markets are experiencing protracted weak growth, which carries the risk of turning into a more structural slowdown, according to an IIF report. Excluding China and India, arguably outliers due to their large populations and economic heft, emerging markets have not materially outgrown advanced economies since 2013. The causes of this growth slump are more immediate and relate to weak investment in crisis economies like Argentina and Turkey, where balance of payment "sudden stops" sharply curtailed investment, and stagnation cases like Mexico and South Africa, where weak investment has been part of a slowing growth trend for some time.

Exhibit 5. Turkey and Argentina are weakest, ...



Source: Haver, IIF

Exhibit 6. ... but many others are weak too.



Source: Haver, IIF

China

The authorities extended the Lunar New Year holiday across a number of regions to halt the spread of the virus. Fourteen provinces announced an extension of the current new year holiday by more than a week and noted that businesses do not need to start operations until at least the second week of February. By Bloomberg's estimate, these cities accounted for nearly 69% of China's 2019 GDP in 2019; extended business disruptions there could pose sizable downside risks to growth. In currencies, **the offshore CNH pulled back from the CNH7/USD level to CNH 6.989/USD** but remains near its weakest level since mid-December**.** By comparison, the onshore CNY, which has not been traded since the start of the Lunar New Year celebration on January 23rd, remains at CNY 6.94/USD. The spread between the offshore and onshore RMB is now at its widest since last August. Chinese onshore markets remain closed until Monday, February 3.

Ghana

The Central Bank of Ghana kept interest rates at 16%, as expected. Governor Addison justifies the MPC's decision given that the economy is "stable" and inflation is forecasted to remain "within the medium-term target band." In fact, this latest decision to hold rates is the sixth consecutive one as inflation has remained within the CB's 6% to 10% target band since April 2018. Inflation was running at 7.9% y/y in December, down from 8.2% in November.

Mexico

Economic growth was close to zero in 2019Q4. On an non-seasonally adjusted y-o-y basis, GDP declined 0.3%, according to the preliminary report, better than expectations for a decline of 0.5%. On a seasonally adjusted quarterly basis, GDP slipped by 0.02% from 3 months earlier. A slight up-tick in services kept the activity from contracting further. The report is seen as supporting market analysts' expectations for a 25 bps rate cut on February 13 by Banxico.

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Global Financial Indicators

Last updated: 1/31/20 8:13 AM	Level: Last 12m	Level: Latest	Change: 1 Day	Change: 7 Days	Change: 30 Days	Change: 12 M	YTD
Equities					%		%
United States		3284	0.3	-1	2	21	2
Europe		3674	-0.5	-3	-2	16	-2
Japan		23205	1.0	-3	-2	12	-2
China		2977	-2.8	-3	0	15	-2
Asia Ex Japan		70	-1.6	-5	-4	2	-4
Emerging Markets		43	-0.2	-4	-4	0	-4
Interest Rates					basis points		
US 10y Yield		1.55	0.2	-13	-37	-108	-37
Germany 10y Yield		-0.42	-1.2	-8	-23	-57	-23
Japan 10y Yield		-0.07	-0.8	-5	-6	-7	-6
UK 10y Yield		0.53	-1.5	-4	-30	-69	-30
Credit Spreads					basis points		
US Investment Grade		108	0.5	5	10	-14	10
US High Yield		437	2.4	23	43	-1	43
Europe IG		46	0.4	1	2	-24	2
Europe HY		230	2.7	10	23	-78	23
EMBIG Sovereign Spread		312	1.0	5	19	-54	19
Exchange Rates					%		
USD/Majors		97.78	-0.1	0	1	2	1
EUR/USD		1.11	0.2	0	-1	-3	-1
USD/JPY		108.9	0.1	0	0	0	0
EM/USD		59.9	-0.3	-1	-2	-7	-2
Commodities					%		
Brent Crude Oil ($/barrel)		59	0.4	-4	-11	-5	-11
Industrials Metals (index)		106	0.1	-5	-7	-10	-7
Agriculture (index)		39	-0.3	-3	-5	-8	-5
Implied Volatility					%		
VIX Index (%, change in pp)		16.8	1.4	2.3	3.1	0.3	3.1
10y Treasury Volatility Index		4.7	-0.1	0.4	0.6	0.9	0.6
Global FX Volatility		5.6	0.0	0.3	-0.4	-2.3	-0.4
EA Sovereign Spreads					10-Year spread vs. Germany (bps)		
Greece		159	1.9	-5	-6	-213	-6
Italy		134	-0.4	-22	-25	-110	-25
Portugal		69	0.3	-2	6	-78	6
Spain		67	-0.9	-1	1	-38	1

Colors denote tightening/easing financial conditions for observations greater than ±1.5 standard deviations.
Data source: Bloomberg.

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Emerging Market Financial Indicators

Last updated: 1/31/2020 8:11 AM	Exchange Rates							Local Currency Bond Yields (GBI EM)						
	Level		Change (in %)					Level		Change (in basis points)				
	Last 12m	Latest	1 Day	7 Days	30 Days	12 M	YTD	Last 12m	Latest	1 Day	7 Days	30 Days	12 M	YTD
		vs. USD	(+) = EM appreciation					% p.a.						
China		6.94	-0.5	-0.9	1	-2	0		3.0	0.0	0	-10	-5	-11
Indonesia		13655	0.0	-0.5	2	2	2		6.8	-0.3	1	-35	-147	-30
India		71	0.2	0.0	0	0	0		6.9	-0.3	-1	-1	-69	-2
Philippines		51	0.3	0.0	0	3	0		4.2	7.0	-4	-5	-153	-8
Thailand		31	-0.1	-1.9	-4	0	-4		1.5	-2.0	-5	-10	-110	-10
Malaysia		4.10	-0.2	-1.0	0	0	0		3.1	-0.8	-2	-23	-92	-23
Argentina		60	0.0	-0.2	-1	-38	-1		57.4	206.3	357	-523	3613	-523
Brazil		4.27	-0.5	-2.0	-6	-15	-6		6.0	2.2	-6	-16	-191	-23
Chile		800	-0.4	-2.7	-6	-18	-6		3.4	2.6	7	12	-106	12
Colombia		3418	-0.1	-1.5	-4	-9	-4		5.7	3.1	-1	-27	-84	-28
Mexico		18.84	-0.3	-0.3	0	1	0		6.7	-1.3	-16	-20	-181	-21
Peru		3.4	-0.7	-1.4	-1	0	-2		4.3	-0.7	-8	-20	-144	-22
Uruguay		38	0.1	-0.7	0	-13	0		10.4	3.5	-6	-47	2	-47
Hungary		305	0.2	0.0	-3	-10	-3		1.3	-2.0	-2	14	-80	12
Poland		3.89	0.0	-0.8	-3	-4	-3		1.9	-3.4	-8	4	-30	4
Romania		4.3	0.1	0.2	-1	-4	-1		3.8	0.0	-5	-15	-57	-16
Russia		63.6	-0.6	-2.4	-3	3	-3		6.0	1.5	6	-11	-206	-11
South Africa		14.9	-1.1	-3.6	-6	-11	-6		9.5	-1.3	-4	-1	4	-3
Turkey		5.98	-0.2	-0.7	-1	-14	-1		9.8	-7.1	-39	-192	-568	-189
US (DXY; 5y UST)		98	-0.1	-0.1	1	2	1		1.38	-2.8	-13	-31	-106	-31

	Equity Markets							Bond Spreads on USD Debt (EMBIG)						
	Level		Change (in %)					Level		Change (in basis points)				
	Last 12m	Latest	1 Day	7 Days	30 Days	12 M	YTD	Last 12m	Latest	1 Day	7 Days	30 Days	12 M	YTD
								basis points						
China		2977	0.0	-3	0	15	-2		171	-8	-4	-5	-16	-5
Indonesia		5940	-1.9	-5	-6	-9	-6		178	-1	9	22	-19	22
India		40723	-0.5	-2	-1	12	-1		132	-1	5	4	-54	7
Philippines		7201	-2.6	-6	-8	-10	-8		78	1	4	12	-20	12
Malaysia		1531	-0.9	-3	-4	-9	-4		112	1	8	0	-28	0
Argentina		40395	0.1	-2	-3	11	-3		2052	3	-29	283	1381	283
Brazil		115528	0.1	-2	0	19	0		223	0	-1	8	-12	8
Chile		4549	-0.5	-2	-3	-16	-3		147	-1	-2	14	0	14
Colombia		1638	0.3	-1	-1	13	-1		175	3	-1	12	-15	12
Mexico		44863	-0.6	-1	3	2	3		305	1	2	13	-25	13
Peru		19915	-0.3	-3	-3	-1	-3		121	1	2	14	-23	14
Hungary		43324	-0.4	-3	-6	6	-6		112	2	11	26	-26	26
Poland		56469	-0.8	-4	-2	-6	-2		39	2	11	21	-31	21
Romania		10020	0.7	-2	0	44	0		195	-2	10	19	-24	22
Russia		3101	-0.2	-1	2	23	2		147	0	-1	16	-77	16
South Africa		56103	-0.9	-2	-2	4	-2		349	2	4	29	39	29
Turkey		119703	-0.1	-2	5	15	5		366	1	-2	-35	-46	-35
Ukraine		510	0.9	1	0	-8	0		398	0	20	-22	-299	-22
EM total		43	-0.2	-4	-4	0	-4		312	1	5	19	-54	19

Colors denote tightening/easing financial conditions for observations greater than ±1.5 standard deviations. Data source: Bloomberg.

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