GLOBAL MARKETS ANALYSIS
Monetary and Capital Markets

Global Markets Monitor

WEDNESDAY, JUNE 15, 2022

- **Markets price in a hawkish outcome for the FOMC meeting** (link)
- **Southern European spreads narrow on news of unscheduled ECB meeting** (link)
- **European gas prices jump amid supply disruptions** (link)
- **China keeps 1-year MLF rate unchanged at 2.85%** (link)
- **Local yields plunge in Turkey in response to authorities' measures** (link)

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Focus on ad-hoc ECB meeting ahead of Federal Reserve

Southern European spreads fell, and equities rose on news of an ad-hoc ECB meeting this morning. In the statement published after this unscheduled meeting, the ECB said that it will apply flexibility in reinvesting redemptions coming due in its pandemic PEPP portfolio to preserve monetary policy transmission. In addition, the ECB Governing Council decided to mandate relevant Committees to accelerate the completion of the design of a new anti-fragmentation instrument. The euro reversed most of its earlier gains following the publication of the statement as contacts point out that the statement provided no details on a new anti-crisis tool. **Meanwhile, investors continued to digest a baseline where the Fed hikes by 75 bps later today.**

Key Global Financial Indicators

Last updated: 6/15/22 1:05 PM	Level		Change from Market Close				
	Last 12m	Latest	1 Day	7 Days	30 Days	12 M	YTD
Equities					%		%
S&P 500		3735	-0.4	-10	-7	-12	-22
Eurostoxx 50		3519	1.3	-7	-5	-15	-18
Nikkei 225		26326	-1.1	-7	-1	-10	-9
MSCI EM		40	1.4	-6	-1	-27	-18
Yields and Spreads					bps		
US 10y Yield		3.37	-10.2	35	45	188	186
Germany 10y Yield		1.65	-11.3	29	70	188	182
EMBIG Sovereign Spread		481	-3	30	12	153	114
FX / Commodities / Volatility					%		
EM FX vs. USD, (+) = appreciation		51.7	0.6	-2	0	-11	-2
Dollar index, (+) = $ appreciation		104.9	-0.6	2	0	16	10
Brent Crude Oil ($/barrel)		120.8	-0.3	-2	8	63	55
VIX Index (%, change in pp)		32.4	-0.3	8	4	15	15

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

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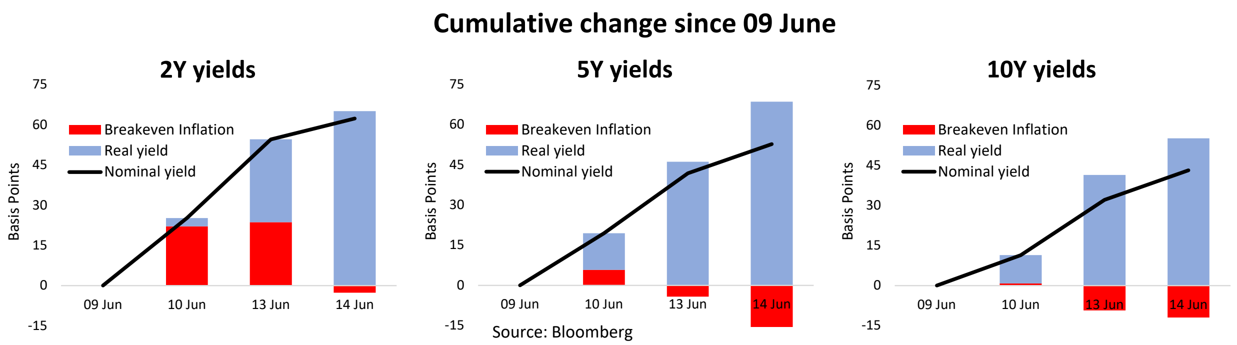
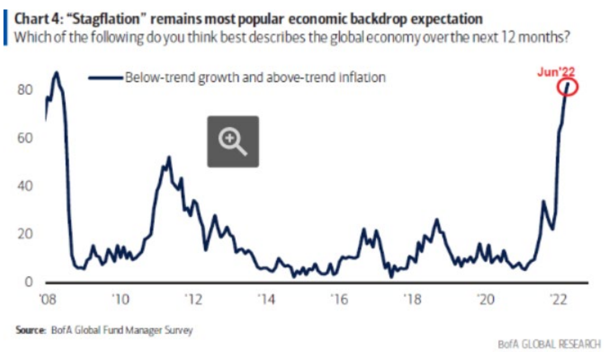
United States

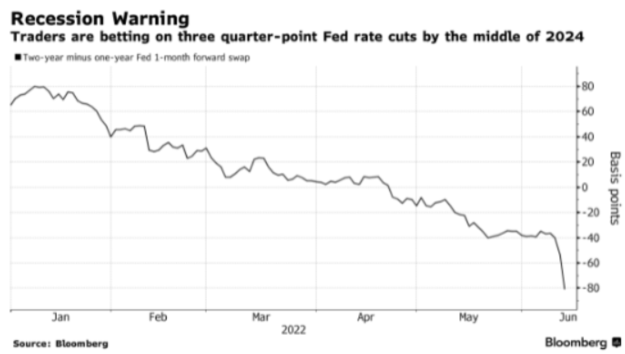
Investors continued to digest a baseline where the Fed hikes by 75 bps today. S&P500 declined by 0.4%. US Treasury real yields continued rising, partially compensated by falling break inflation: UST 10-yr nominal yield grew by 11 bps. Correspondingly, the US dollar appreciated versus major (+0.4%) and emerging market (+0.5%) currencies.

Markets have priced in relatively more hawkish tightening by the Fed in recent days, with no additional inflationary risks in the short run. Even though last Friday's inflation surprise initially led to a spike in 2-yr breakeven inflation on Friday and Monday (left chart below), the consensus as of Tuesday was that the Fed will be committed to fight inflation at any cost. **While the new consensus for the June's rate hike stays at 75 bps, some economists do not rule out a possibility of a 100-bps hike. The nominal yields for all tenors increased dramatically in recent days, driven by a large (60–70 bps) increase in real yields.**



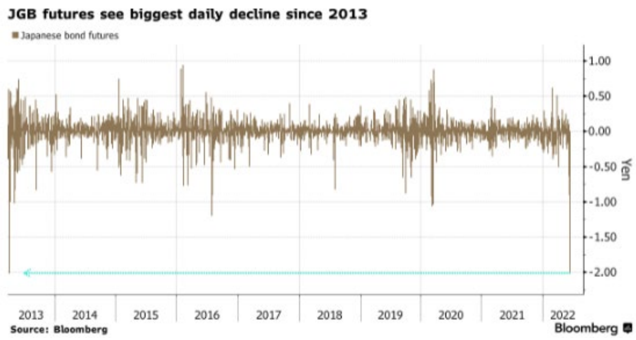
Markets pay more attention to post-inflationary policy rate normalization in 2023–2024. A recent survey by the Bank of America shows that the vast majority of respondents fear that the most probable outlook for the next 12 months is a combination of *below-trend growth* and *above-trend inflation*—the highest number of such responses since 2008 (left chart below). Markets are convinced that in order to avoid the emergence of a full-blown stagflation from the current conditions, the Fed would have to act promptly—meaning that the sharp rise in the policy rate will have to be short lived and the consequent policy rate normalization may start already in 2024 (or even earlier). **Correspondingly, interest rate derivatives price in that there will be about 3 quarter-point policy rate cuts between the mid-2023 and the mid-2024 (right chart showing the difference between the policy rate 2-years ahead and the policy rate 1-year ahead).**





Japan

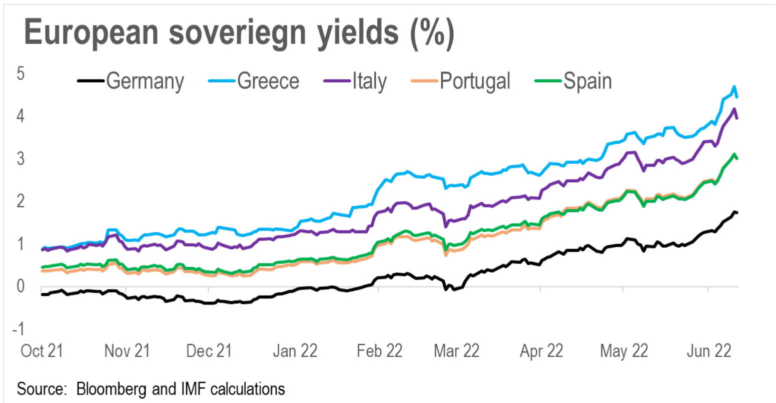
Traders are betting that the Bank of Japan will be forced to abandon its pledge to cap yields at 0.25%. Ten-year bond futures slumped by the most since 2013 on Wednesday, Bloomberg reports. The selloff persisted even after the BOJ expanded its bond buying program and announced unlimited purchases of cheapest-to-deliver 10-year notes. Relatedly, MUFG now sees higher upper trading ranges for ultra-long yields, which recently surged on rising US yields and speculation of BOJ policy tweaks aimed at tackling excessive yen depreciation. **Equities slid -1.2%, the yen recovered +0.6%**,**10-year yields climbed +0.7 bps** to just below BOJ's 0.25% ceiling.



Euro area

Southern European spreads remain significantly below yesterday's levels but widened somewhat following the release of a statement after today's unscheduled ECB meeting. In the statement, the ECB said that it will apply flexibility in reinvesting redemptions coming due in the PEPP portfolio to preserve the functioning of the monetary policy transmission mechanism. In addition, the Governing Council decided to mandate relevant Eurosystem Committees to accelerate the completion of the design of a new anti-fragmentation instrument. **The euro reversed most of its earlier gains posted following the publication of the statement.**

The spreads between Italian and German 10-yr yields narrowed by 21 bps to 221 bps, remaining roughly +17 bps higher than before last week's ECB meeting. Markets are now pricing roughly +187 bps of tightening in 2022.

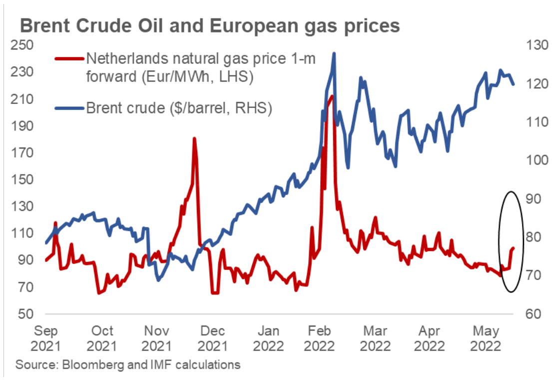


Source: Bloomberg and IMF calculations

Equities (+1%) traded higher, breaking a 2-day losing streak. The banking sector (+3.8%) outperformed, while the energy sector (-1%) saw the largest losses. **The euro strengthened (+0.8%) and sovereign yields fell, and peripheral spreads narrowed on news that the ECB Governing Council will have an ad-hoc meeting today to discuss market conditions.**

Industrial production data disappointed, falling 2.0% yoy in April (vs expected -1.1% from -0.5%). Industrial production increased by +0.4% on a monthly basis in April (vs expected +0.5% mom from -1.4%). Separately France's final May inflation print was in line with previous estimates (EU harmonized measure +5.8% yoy).

Natural gas prices in Europe jumped yesterday (+15%) and saw further upward momentum this morning (benchmark 1-month forward +2% to €99/MwH) as supply concerns intensified. Gazprom reported that a technical issue is limiting supply via the Nord Stream pipeline—the largest link to the EU—by 40%. Prices were also boosted by news that a Texas export terminal would take three months to repair after an explosion last week, extending the previous assessment that the damage would take three weeks to repair. Analysts caution that these constraints make it more difficult for Europe to meet its storage targets and warned of persistent high prices in Europe this winter as a result.



Emerging Markets

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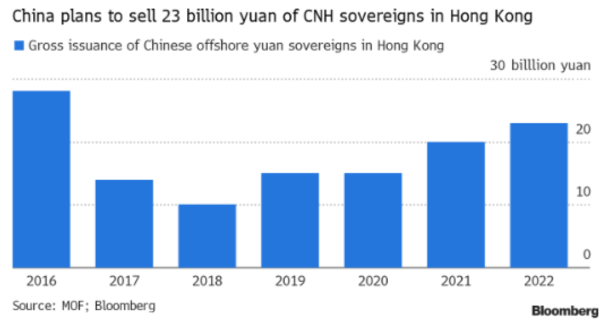
Asian equities were little changed. Stock markets rallied in Mainland China (CSI +1.3%) and Hong Kong SAR (+1.1%). The Philippines (-2.4%), South Korea (-1.8%), and Malaysia (-1.5%) declined. **Asian currencies were mixed.** Chinese renminbi strengthened (+0.4%) on no change in monetary policy settings; Philippine peso depreciated (-0.4%), followed by Thai baht (-0.3%), Indonesian rupiah (-0.3%), and South Korean won (-0.3%) weakened. **10-year yields increased,** led by Australia (+24.5 bps) and the Philippines (+13.4 bps). **The rebound in EMEA equities continued today, with all main markets gaining, except Poland (-0.7%).** The rebound is Hungary is particularly strong (+1.8%), and the forint is also appreciating (+0.7% to 398.7/euro) in a continuation of yesterday's trends. Elsewhere in CEE, the Polish zloty is losing (-0.3% to 4.67/euro) currencies are broadly unchanged vs. the euro, while the South African Rand and Turkish lira are broadly flat against the dollar. Equities closed lower in Peru (-1.4%), Mexico and Argentina (-0.6%), and Brazil (-0.5%), while currencies weakened in Chile (-0.8%), Mexico (-0.7%), Peru (-0.4%), and Argentina (-0.2%). Colombian assets deviated from the regional trend, with equities gaining 1.2% and the peso remaining flat, as an outperforming electricity provider pushed the local stock index higher and coffee prices (+1.5%) provided additional support on the commodity front. The region's hard and local currency treasury yield curves followed once again the upward shift in US rates.

China

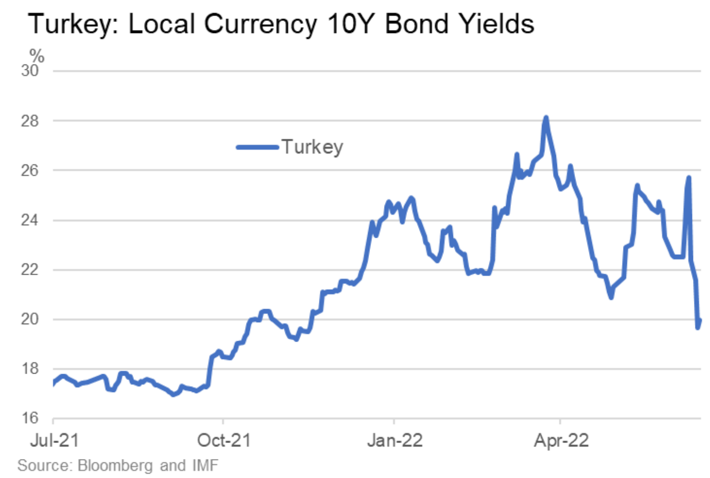
People's Bank of China's (PBOC) kept its 1-year lending facility rate at 2.85%, as expected. The PBOC also rolled over the 200 bn yuan ($29.7 bn) of maturing medium-term lending facility (MLF) loans. Meanwhile analysts believe PBOC will continue with easing bias and cut the MLF rate later this year together with lower reserve requirement ratio. Separately, **China's offshore sovereign bond sale saw strong demand.** The Ministry of Finance placed 7.5 bn yuan ($1.1 bn) across two, three and five-year maturity, which became the largest sale in six years and is part of 23 bn yuan issuances planned for this year in Hong Kong. Bid-to-cover ratio stood at 4.6 reached, the highest since July 2020, according to

Bloomberg. Separately, **China's activity data broadly improved in May**. Decline moderated for industrial production (-0.7% y/y; previous: -2.9%) and retail sales (-6.7% y/y, previous: -11.1%) amid eased COVID measures in Shanghai. However, fixed asset investment growth slowed to 6.2% y/y ytd (previous: 6.8%). **Equities continued to rally (CSI 300 +1.32%), 10-year yields firmed +0.7 bps, renminbi strengthened (onshore: +0.3%, offshore: +0.4%).**



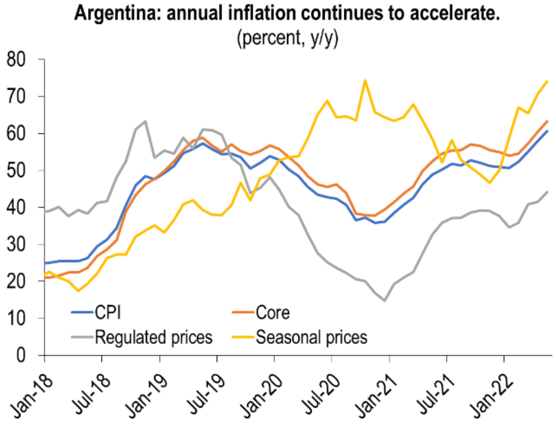
Turkey

In sharp contrast to regional trends, yields on 10-yr local currency have collapsed 573 bps since last Friday when the authorities announced measures to support the lira, and in particular the new revenue-indexed bonds. Demand collection for these bonds will start today. These bonds are aimed at retail investors and designed to encourage investment in lira-denominated assets and shore up the currency. They will have a 182 day maturity and a quarterly coupon rate of 5.32% (23.04% annualized), which will be adjusted on the revenue realizations of two SOEs to whose earnings the bonds are indexed. **Analysts doubt that these bonds will manage to stabilize the lira (which has depreciated 23% to the US dollar in 2022 so far).**



Argentina

Argentina's sovereign debt markets calmed down, while yesterday's inflation print still generated expectations for rate hikes. Inflation printed in May with 60.7% y/y, 10 bps higher than expected and 2.7 ppt above the April value, even if slowing down by 90 bps at the monthly margin. Core inflation increased as much as the headline rate, printing at 63.2%. Economists surveyed by the central bank anticipate an inflation rate of 72.6% for end-of 2022 and analysts expect a 200 bps hike in the policy rate to a level of 51%, possibly on Thursday this week. Meanwhile the recent slump in the country's treasuries ended, as the government auctioned yesterday successfully $180 mn in local currency notes, with a second auction to follow today. The peso's depreciation in parallel markets slowed down to 1%.



Source: Bloomberg.

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Global Financial Indicators

Last updated: 6/15/22 1:07 PM	Level: Last 12m	Level: Latest	Change: 1 Day	Change: 7 Days	Change: 30 Days	Change: 12 M	YTD
Equities					%		%
United States		3745	-0.4	-9	-7	-12	-21
Europe		3519	1.3	-7	-5	-15	-18
Japan		26326	-1.1	-7	-1	-10	-9
China		3305	0.5	1	8	-6	-9
Asia Ex Japan		69	1.6	-5	1	-27	-17
Emerging Markets		40	1.4	-6	-1	-27	-18
Interest Rates					basis points		
US 10y Yield		3.37	-10.2	35	45	188	186
Germany 10y Yield		1.65	-11.3	29	70	188	182
Japan 10y Yield		0.26	0.7	1	1	21	19
UK 10y Yield		2.46	-12.3	22	72	171	149
Credit Spreads					basis points		
US Investment Grade		163	1.1	12	-2	72	51
US High Yield		505	12.9	62	23	179	167
Europe IG		105	-3.8	14	11	57	57
Europe HY		523	-20.9	68	72	287	281
Exchange Rates					%		
USD/Majors		104.92	-0.6	2	0	16	10
EUR/USD		1.05	0.3	-2	0	-14	-8
USD/JPY		134.6	-0.6	0	4	22	17
EM/USD		51.7	0.6	-2	0	-11	-2
Commodities					%		
Brent Crude Oil ($/barrel)		121	-0.3	-2	8	63	55
Industrials Metals (index)		174	1.0	-7	-2	12	1
Agriculture (index)		75	-0.3	-2	-3	32	23
Implied Volatility					%		
VIX Index (%, change in pp)		32.4	-0.3	8.4	3.5	15.4	15.2
US 10y Swaption Volatility		136.9	-0.9	32.4	19.7	70.9	57.9
Global FX Volatility		11.9	0.0	1.5	0.7	5.3	4.4
EA Sovereign Spreads					10-Year spread vs. Germany (bps)		
Greece		262	-33.0	0	8	164	110
Italy		217	-25.2	15	26	115	82
Portugal		124	-11.5	9	12	62	59
Spain		125	-10.7	12	20	61	51

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

Emerging Market Financial Indicators

Last updated: 15/06/2022 1:09 PM	Exchange Rates: Level, Last 12m	Level, Latest (vs. USD)	Change (in %) ((+) = EM appreciation): 1 Day	7 Days	30 Days	12 M	YTD	Local Currency Bond Yields (GBI EM): Level, Last 12m	Level, Latest (% p.a.)	Change (in basis points): 1 Day	7 Days	30 Days	12 M	YTD
China		6.71	0.5	-0.3	1	-4	-5		2.9	1.5	3	3	-36	4
Indonesia		14745	-0.3	-1.7	0	-4	-3		7.4	0.8	26	5	103	105
India		78	-0.1	-0.4	0	-6	-5		6.3	0.0	0	9	75	0
Philippines		53	-0.4	-1.0	-2	-10	-5		5.7	22.5	23	28	158	120
Thailand		35	0.1	-1.3	-1	-11	-5		3.0	5.0	15	-32	115	116
Malaysia		4.41	0.2	-0.4	0	-7	-6		4.3	-5.5	12	-9	105	74
Argentina		123	-0.2	-1.0	-4	-22	-16		60.9	66.0	450	772	1530	1034
Brazil		5.10	0.3	-4.0	-1	-1	9		13.3	12.9	56	96	409	260
Chile		868	-0.8	-4.7	-1	-17	-2		6.6	0.0	27	28	273	120
Colombia		3968	0.2	-4.6	2	-8	2		9.3	0.0	46	24	365	291
Mexico		20.57	0.1	-4.8	-3	-3	0		9.3	4.0	42	63	248	175
Peru		3.8	-0.4	-0.2	0	4	6		8.0	0.1	30	10	261	212
Uruguay		40	-0.2	-1.1	3	9	11		10.9	0.0	43	81	311	221
Hungary		381	0.9	-3.1	-2	-24	-15		8.2	0.0	91	118	558	369
Poland		4.47	0.1	-4.2	0	-16	-10		7.5	7.5	82	135	571	394
Romania		4.7	0.3	-2.5	0	-14	-8		8.7	40.0	65	77	599	389
Russia		56.4	3.6	6.9	14	28	33		8.4	1.7	31	-291	104	-38
South Africa		16.0	0.1	-4.6	1	-14	-1		8.8	-16.5	19	32	163	140
Turkey		17.30	-0.2	-0.9	-10	-51	-23		19.9	23.0	-543	-529	168	-444
US (DXY; 5y UST)		105	-0.5	2.4	0	16	10		3.47	-12.2	43	60	268	220

	Equity Markets: Level, Last 12m	Level, Latest	Change (in %): 1 Day	7 Days	30 Days	12 M	YTD	Bond Spreads on USD Debt (EMBIG): Level, Last 12m	Level, Latest (basis points)	Change (in basis points): 7 Days	30 Days	12 M	YTD
China		4278	1.3	1	8	-16	-13		186	-13	-22	-23	-17
Indonesia		7007	-0.6	-3	6	15	6		183	-2	-25	13	18
India		52541	-0.3	-4	-1	0	-10		174	9	-11	29	42
Philippines		6319	-2.4	-7	-3	-9	-11		126	-1	-33	33	25
Malaysia		1459	-1.5	-4	-6	-8	-7		121	-2	-14	-3	4
Argentina		87400	-0.6	-4	-2	30	5		2129	198	235	673	449
Brazil		102063	0.0	-7	-5	-22	-3		331	21	23	82	20
Chile		5121	0.0	-3	6	17	19		166	15	-3	17	26
Colombia		1501	1.1	-4	-1	20	6		396	52	13	155	48
Mexico		48164	-0.6	-4	-3	-5	-10		422	38	39	95	90
Peru		19563	-1.4	-5	-1	2	-7		192	18	2	28	42
Hungary		39505	2.1	-2	-4	-20	-22		216	-5	12	76	92
Poland		52714	-1.0	-6	-4	-21	-24		69	0	67	32	37
Romania		12113	0.4	-3	0	4	-7		280	29	45	103	87
Russia		2310	0.9	1	0	-40	-39		3411	-577	938	3228	3234
South Africa		66585	1.4	-5	-3	-1	-10		436	48	23	131	81
Turkey		2510	0.1	-1	4	74	35		675	81	73	224	97
Ukraine		519	0.0	0	0	-2	-1		3640	264	233	3166	2881
EM total		40	0.9	-6	-1	-27	-18		415	30	4	69	28

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

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