



- **US debt ceiling back in focus** ([link](#))
- **Equities in US underperformed peers in August** ([link](#))
- **Investors in US corporate bonds face greater risks** ([link](#))
- **China's local governments to launch offshore bonds** ([link](#))
- **German IFO survey confirms slowing economic momentum** ([link](#))
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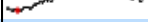

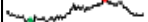

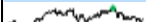



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## Quiet summer trade continues

**Markets remain quiet in the midst of the August summer holidays, with US equity futures holding steady and European markets mixed but little changed.** The recent rally in Chinese technology stocks came to an end as worries about government crackdowns persisted. The recent uptick in US Treasury yields continues this morning, with the benchmark 10-year Treasury yield hitting rising above 1.30% for the first time in two weeks. The currency markets are holding steady, while commodities posted minor gains. Volatility remains subdued. Strong corporate earnings, rising vaccination rates and continued monetary policy support have buoyed sentiment in recent days, as many equity indexes trade at or near their all-time highs. Attention now shifts to the US Federal Reserve's Jackson Hole conference, which begins tomorrow. Few expect any major policy announcements ahead of next month's FOMC meeting.

Key Global Financial Indicators

Last updated: 8/25/21 8:11 AM	Level		Change from Market Close				YTD
	Last 12m	Latest	1 Day	7 Days	30 Days	12 M	
<b>Equities</b>			%				%
S&P 500		4486	0.1	1	2	30	19
Eurostoxx 50		4182	0.1	0	2	26	18
Nikkei 225		27725	0.0	1	0	19	1
MSCI EM		51	2.3	2	-2	14	-1
<b>Yields and Spreads</b>			bps				
US 10y Yield		1.30	0.8	4	3	62	39
Germany 10y Yield		-0.45	3.1	4	-3	-2	12
EMBIG Sovereign Spread		348	-5	-5	-5	-70	-2
<b>FX / Commodities / Volatility</b>			%				
EM FX vs. USD, (+) = appreciation		56.2	-0.1	0	0	2	-3
Dollar index, (+) = \$ appreciation		93.0	0.1	0	0	0	3
Brent Crude Oil (\$/barrel)		71.6	0.8	5	-3	56	38
VIX Index (% change in pp)		17.4	0.2	-4	0	-5	-5

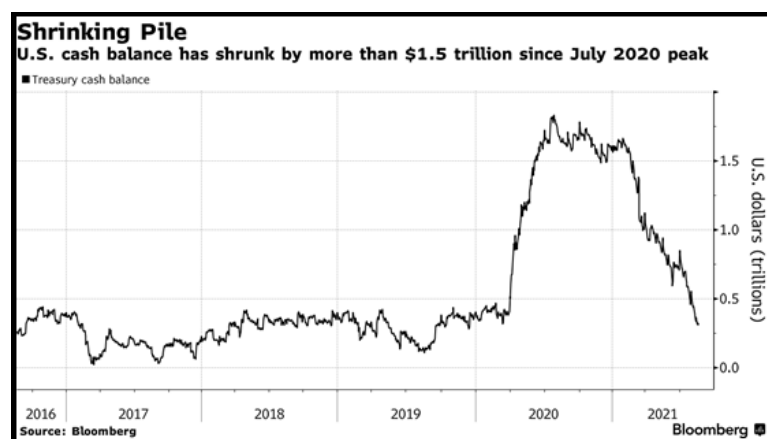
Colors denote **tightening/easing** financial conditions for observations greater than  $\pm 1.5$  standard deviations. Data source: Bloomberg.

## Mature Markets

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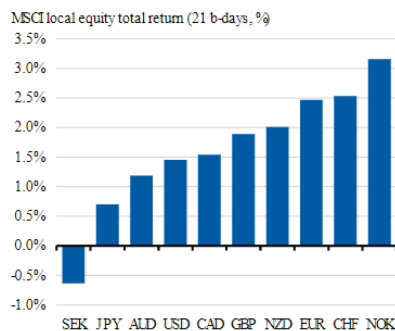
### United States

**The US debt ceiling is coming back into focus for September as the Treasury Department's cash holdings have declined to \$310 bn.** This is the lowest since the pandemic began. The debt ceiling was reinstated on August 1 at \$28.5 trillion following its suspension back in July 2019. Treasury is currently employing "emergency measures" to save cash so that the government can meet its obligations, but back in July the Congressional Budget Office estimated that the "X-Date" when the government runs out of cash could occur in October or November. If the debt ceiling is not raised in time a default could be triggered. S&P took away the US' AAA rating on August 5, 2011, downgrading it to AA+, when a default seemed imminent due to political disagreements. With the debate over the President's \$3.5 tn spending package underway, there is a chance that political opponents could use the debt ceiling as negotiating tactic, raising the chance of a miscalculation and another fiscal crisis.



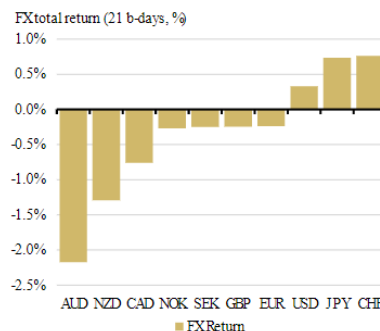
**US equities have done worse than many developed marked peers so far in August.** The S&P 500 is up just 2.3% compared to stocks in the euro area, Switzerland, and Norway. This is a reversal from recent years, when the US did much better than most other advanced economies. On a year-to-date and local currency basis, the US is being outperformed by France's CAC-40 and Sweden's OMX, but it leads most other advanced economy bourses. However, on the currency front, the dollar has done better than its peers with the exception of the yen and Swiss franc, which are considered to be safe haven currencies.

**Exhibit 3:** Performance of local equity indices during the month so far



Source: Macrobond, Bloomberg, Morgan Stanley Research

**Exhibit 4:** Performance of each currency versus USD during the month so far



Source: Macrobond, Bloomberg, Morgan Stanley Research

The latest US durable goods data were stronger than expected. Both the headline number and the more closely followed ex-transportation number came in ahead of forecasts. Markets were unchanged following the numbers.

## US Durable Goods for July 2021

Source: Bloomberg

	Forecast	Actual Data	June Revision
Durable goods	-0.3%	-0.1%	+0.8% from +0.9%
Durables ex-transportation	+0.5%	+0.7%	+0.6% from +0.5%

**Investors in US corporate bonds face rising risks.** JP Morgan points out credit spreads for both investment grade (IG) and high yield (HY) have now fallen below pandemic levels. In addition, the analysts estimate that US non-bank investors are overweight corporate bonds by nearly 30%, the highest in many years. In this situation, investors are extremely vulnerable to a sharp reversal in spreads. The extremely low level of interest rates also presents a threat, as investors face the risk of an interest rate shock if their portfolios are unhedged, as many are. Bonds issued in recent years have very low coupons due to the low level of rates, and low coupon bonds are much more sensitive to interest rate shocks than bonds with higher coupons.

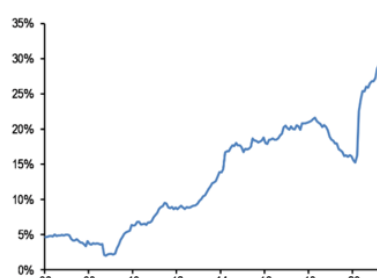
Figure 9: US HG and Global HY credit spread vs. government bonds (bps)



Source: J.P. Morgan.

Figure 10: Implied credit overweight by US non-bank investors

Percentage of non-government bonds in non-bank US investors' bond portfolios minus percentage of non-government bonds in the tradable bond universe of the US Agg bond index augmented by US HY corporate bonds, Munis, and inflation linked bonds.



Source: J.P. Morgan.

## Euro Area

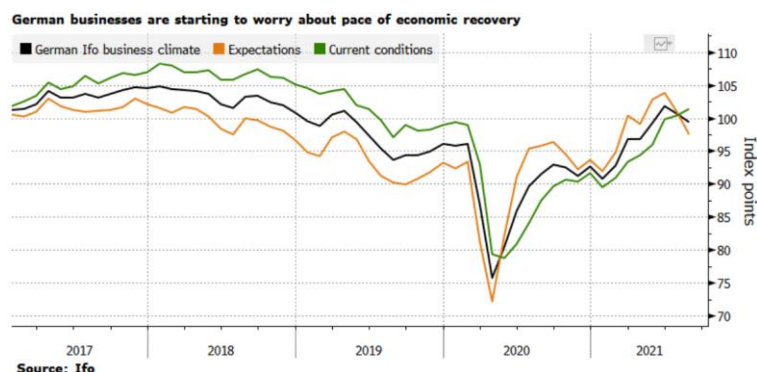
**European equities** were trading marginally higher this morning with Euro STOXX 600 benchmark up 0.2%. Travel and leisure sector continued recover, gaining well above the market (+2%). **European bond yields** were up 3 bps with German 10-year bund trading at the top of the August range. Southern European spreads were steady, except for Italy which widened by 2 bps in the 10-year sector. The bond yield increase gained momentum after ECB's Vice President Guindos indicated that the ECB's next forecast could signal an improved growth outlook.



**ECB Executive Board member Schnabel highlighted the need for tighter regulation in the non-bank financial sector** as their increasing exposure to duration, liquidity and credit risk could impair central bank policy during periods of stress. She also noted that while higher holdings of financial assets by non-banks

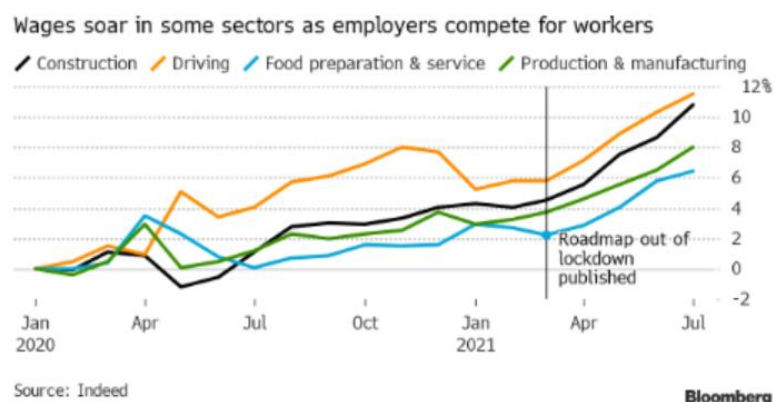
may have strengthened the effectiveness of central bank assets purchases, the various level of developments of non-bank financial sector across the Euro area could translate to uneven policy effects.

On the data front, **the German IFO release confirmed the slowing of the recovery momentum** as the business climate and expectations gauge declined by more than consensus had expected. Analysts noted that the release is consistent with the earlier PMI readings and while Q3 GDP growth should remain solid, softer surveys create some uncertainty for Q4 and beyond.



## United Kingdom

**Parts of the UK's labor market continue to experience staff shortages** according to job advertisement data by Indeed. Among the worst affected sectors are driving and construction, which have also responded with large wage increase in their job offers. **Contacts noted that the underlying wage growth rate in June stood somewhat above the Bank of England own estimates** and the ongoing labor shortages indicate that wage growth may remain elevated for longer than currently projected by the central bank.



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**Most of Asia was higher but other emerging markets were mixed in the face of differing outcomes with regard to the virus.** In Indonesia, 10-year yield declined further on expectations that direct purchases of government bonds by the central bank will significantly reduce the supply at primary auctions. Higher prices for energy, industrial metals, soybean products and some other agricultural commodities were among the catalysts for the rally in some of Latin America's asset markets. In El Salvador, the rollout of Bitcoin as legal tender continues.

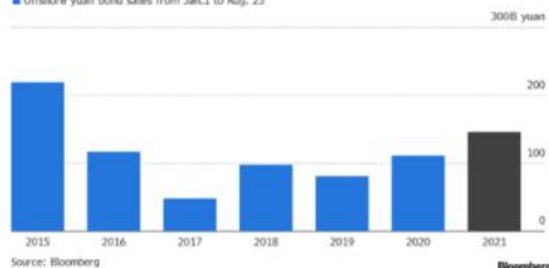
## China

**China's local governments plan to launch offshore yuan bonds.** The Shenzhen city government stated on Tuesday that it is seeking underwriters for an offering of up to 5bn yuan (\$771 mn), while Guangdong

province is also planning such a sale in Macau, without giving the size, according to Bloomberg. Offshore yuan debt sales are on track for the highest since 2015. The proposed offshore sales come amid concerns of a surge in local government bond sales onshore, as Chinese authorities pledge more support for the economy. Overseas investors' holdings of onshore local debt have increased significantly by nearly 80% this year as of July, Bloomberg estimates. Separately, **China's central bank boosted its injection of short-term cash into the financial system**. The People's Bank of China (PBOC) added 50bn yuan (\$7.7bn) of liquidity through its seven-day reverse repo on Wednesday. That resulted in a net injection of 40bn yuan, the largest amount since February. Short-term interbank rate dropped for the first time in five days, while sovereign bonds rose in both futures and cash markets, Bloomberg reports.

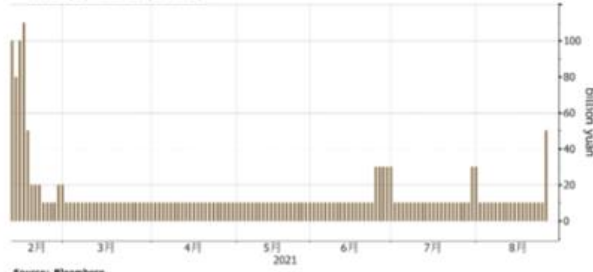
Dim Sum bond sales are set for the highest since 2015

■ Offshore yuan bond sales from Jan.1 to Aug. 25



PBOC injection via reverse repo jumped to highest since early February

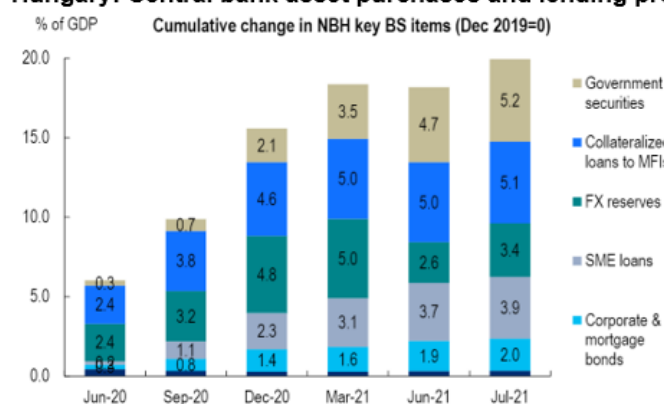
■ PBOC's daily injection via 7-day reverse repo



## Hungary

The forint edged higher but equities (-1%) fell after the National Bank of Hungary (NBH) hiked its policy rate 30 bps to 1.5% (as expected) and decided to gradually withdraw asset purchases. The NBH will reduce asset purchases from a weekly amount of HUF 60 bn to HUF 50 bn, and then set weekly purchases on a quarterly basis from September onwards. The NBH also intends to hike every month until the outlook for inflation stabilizes around the central bank target. According to NBH expectations, inflation will fall below the 4% upper edge of the tolerance band in 2022Q1. Analysts at Citi argue that the NBH's balance sheet policy is likely to remain expansionary given an extension in the corporate bond purchase program and a new green mortgage bond purchase program. **So far this month, the Hungarian forint gained 3% against the euro and equities are up 5.4%.**

### Hungary: Central bank asset purchases and lending programs

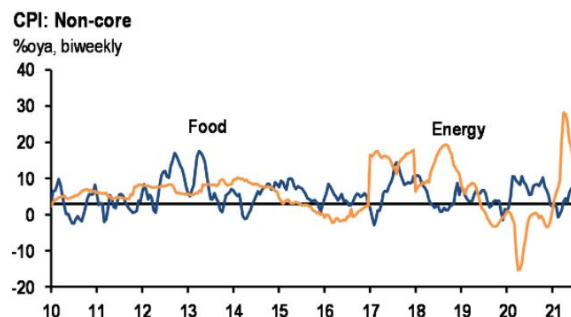
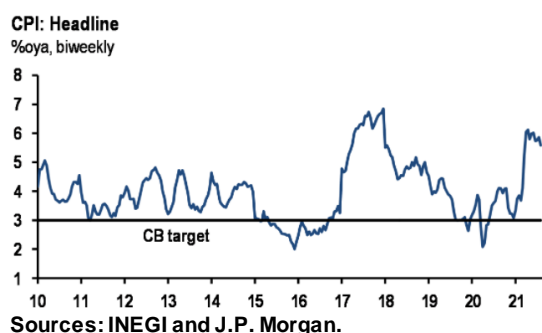


## Mexico

Inflation print leaves inflationary momentum unchanged. Preliminary inflation data for the last two weeks came in at 5.58% yoy, 8 bps lower than expected and 28 bps lower than two weeks ago. Core inflation, which excludes energy and food prices, however, stood at 4.78% yoy, 10bps higher than two weeks before. Lower energy prices sent headline and core inflation in different directions, as the administration lowered



controlled prices for liquefied gas by 15% in the last two weeks. Inflationary momentum thus persists, underscoring expectations for continued hikes in the policy rate which stands currently at 4.5%. Market-implied policy rates reacted modestly, increasing by 1 bps over the one-month horizon and by 5 bps, to 4.92%, over the three-month horizon, while the peso strengthened (+0.5%) and Mexican stocks and sovereign bonds fell back.



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## Global Financial Indicators

Last updated: 8/25/21 8:17 AM	Level		Change				YTD
	Last 12m	Latest	1 Day	7 Days	30 Days	12 M	
Equities			%				%
United States		4487	0.1	2	2	30	19
Europe		4182	0.1	0	2	26	18
Japan		27725	0.0	1	0	19	1
China		3540	0.7	2	2	6	2
Asia Ex Japan		87	2.2	2	-3	10	-3
Emerging Markets		51	2.3	2	-2	14	-1
Interest Rates			basis points				
US 10y Yield		1.30	0.8	4	3	62	39
Germany 10y Yield		-0.45	3.1	4	-3	-2	12
Japan 10y Yield		0.02	0.5	0	1	-1	0
UK 10y Yield		0.57	3.2	1	-1	31	37
Credit Spreads			basis points				
US Investment Grade		94	0.1	0	2	-36	-1
US High Yield		334	-0.5	-10	4	-180	-46
Europe IG		46	0.0	-1	-1	-9	-2
Europe HY		232	0.3	-3	-2	-96	-9
Exchange Rates			%				
USD/Majors		93.03	0.1	0	0	0	3
EUR/USD		1.17	-0.2	0	-1	-1	-4
USD/JPY		109.9	0.3	0	0	3	6
EM/USD		56.2	-0.1	0	0	2	-3
Commodities			%				
Brent Crude Oil (\$/barrel)		72	0.8	5	-3	56	38
Industrials Metals (index)		160	0.7	3	1	37	20
Agriculture (index)		58	-0.3	-2	0	54	20
Implied Volatility			%				
VIX Index (% change in pp)		17.4	0.2	-4.2	0.2	-4.6	-5.4
US 10y Swaption Volatility		75.2	-0.7	3.5	-7.3	17.4	15.1
Global FX Volatility		6.8	0.0	0.1	0.1	-2.3	-1.3
EA Sovereign Spreads			10-Year spread vs. Germany (bps)				
Greece		106	0.0	3	-2	-47	-14
Italy		107	1.8	3	3	-39	-5
Portugal		62	0.9	3	0	-22	2
Spain		72	0.4	2	3	-10	10

Colors denote **tightening**/**easing** financial conditions for observations greater than  $\pm 1.5$  standard deviations. Data source: Bloomberg.

## Emerging Market Financial Indicators

Last updated: 8/25/2021 8:20 AM	Exchange Rates							Local Currency Bond Yields (GBI EM)						
	Level		Change (in %)				YTD	Level		Change (in basis points)				YTD
	Last 12m	Latest	1 Day	7 Days	30 Days	12 M		Last 12m	Latest	7 Days	30 Days	12 M		
	vs. USD		(+) = EM appreciation					% p.a.						
China		6.48	-0.1	0.1	0	7	1		3.0	-3	-4	-16	-26	
Indonesia		14398	0.0	-0.2	1	2	-2		6.2	-6	-7	-43	14	
India		74	-0.1	0.0	0	0	-2		6.4	-2	-2	21	48	
Philippines		50	0.5	1.1	1	-3	-4		4.3	0	-4	70	67	
Thailand		33	0.4	1.6	0	-4	-9		1.6	5	-2	18	33	
Malaysia		4.20	0.3	0.8	1	-1	-4		3.3	1	10	91	76	
Argentina		97	0.0	-0.2	-1	-24	-14		45.6	59	103	122	-1055	
Brazil		5.26	-0.3	2.4	-2	5	-1		9.7	1	117	433	412	
Chile		783	0.3	1.0	-3	0	-9		4.7	7	38	220	196	
Colombia		3866	0.3	0.4	1	0	-11		6.9	1	12	162	179	
Mexico		20.26	-0.3	-1.1	-1	8	-2		7.0	-7	-5	100	141	
Peru		4.1	0.2	-0.1	-4	-12	-12		6.5	-2	97	229	286	
Uruguay		43	0.2	0.8	2	0	-1		7.9	-2	-2	-38	64	
Hungary		297	-0.3	0.7	3	0	0		2.4	8	13	66	84	
Poland		3.90	-0.2	-0.2	0	-5	-4		1.1	1	7	29	48	
Romania		4.2	-0.1	0.1	-1	-3	-5		3.2	1	21	-44	48	
Russia		73.8	-0.1	0.0	0	2	0		6.9	7	6	114	117	
South Africa		15.0	0.2	0.1	-1	13	-2		9.7	-6	-19	-47	2	
Turkey		8.42	-0.1	0.6	2	-12	-12		17.3	-5	-31	357	416	
US (DXY; 5y UST)		93	0.2	-0.1	0	0	3		0.80	3	9	51	44	

	Equity Markets							Bond Spreads on USD Debt (EMBIG)						
	Level		Change (in %)				YTD	Level		Change (in basis points)				YTD
	Last 12m	Latest	1 Day	7 Days	30 Days	12 M		Last 12m	Latest	7 Days	30 Days	12 M		
								basis points						
China		4898	0.2	0	-1	4	-6		218	-3	7	-11	-11	
Indonesia		6113	0.4	0	0	14	2		181	-2	-2	-47	-19	
India		55944	0.0	0	6	43	17		148	-3	-8	-69	-3	
Philippines		6822	2.1	2	7	15	-4		111	-4	-2	-20	-1	
Malaysia		1570	1.1	3	4	1	-4		136	-2	-3	-33	1	
Argentina		71354	3.3	5	10	53	39		1532	-42	-33	-564	176	
Brazil		120211	2.3	2	-4	18	1		296	4	18	-34	37	
Chile		4369	0.0	1	4	12	5		142	-6	-13	-42	-14	
Colombia		1328	-0.5	0	6	8	-8		285	1	9	31	70	
Mexico		51985	-0.1	1	3	36	18		357	-2	3	-105	0	
Peru		17034	5.1	4	-8	-7	-18		176	-8	7	16	47	
Hungary		51213	-0.8	-1	8	44	22		131	-2	-10	-23	-18	
Poland		69281	0.3	1	3	33	21		33	-2	-4	-1	5	
Romania		12332	1.1	2	4	40	26		183	-1	-8	-80	-20	
Russia		3878	-0.3	-1	4	28	18		168	-3	-12	-45	-11	
South Africa		67343	-0.2	-1	-1	20	13		353	1	6	-144	-31	
Turkey		1459	-0.5	1	8	34	-1		466	-6	-10	-155	19	
Ukraine		526	0.0	0	0	5	5		506	-6	-8	-124	13	
EM total		51	0.1	2	-2	14	-1		360	-4	-7	-36	21	

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

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