GLOBAL MARKETS ANALYSIS
Monetary and Capital Markets

Global Markets Monitor

WEDNESDAY, AUGUST 21, 2024
LEAD EDITOR: SANJAY HAZARIKA

- **Investors expect lower short term rates in the next 12 months** (link)
- **US credit markets continue recovery from summer selloff** (link)
- **Hedge funds switch from Yen to dollar as funding currency for carry trades** (link)
- **Institutional investors turn bullish on Yen** (link)
- **Mexico markets samurai bonds for the first time in two years** (link)

Mature Markets | Emerging Markets | Market Tables

Markets are in wait and see mode

Markets are holding steady ahead of key US jobs data today and Fed Chair Powell's Jackson Hole speech on Friday. Stocks in Europe are up and US equity index futures are posting modest gains. At 10am, the US Bureau of Labor Statistics will release revised data on US jobs and some analysts think that 600K fewer jobs were created through March compared to current estimates, with some forecasts as high as a million jobs. The data could have an impact on the Fed's future rate cuts. Short term interest rate futures markets predict nearly 100 bs of rate cuts by December. This afternoon's FOMC minutes could also have an impact on markets. In other news, central banks in Thailand (2.5%) and Indonesia (6.25%) stayed on hold as expected.

Key Global Financial Indicators

Last updated: 8/21/24 7:52 AM	Level		Change from Market Close				
	Last 12m	Latest	1 Day	7 Days	30 Days	12 M	YTD
Equities					%		%
S&P 500		5597	-0.2	3	2	27	17.34
Eurostoxx 50		4885	0.6	3	1	16	8
Nikkei 225		37952	-0.3	4	-4	19	13
MSCI EM		43	-0.8	2	2	13	8
Yields and Spreads					bps		
US 10y Yield		3.81	0.6	-2	-43	-53	-7
Germany 10y Yield		2.21	-0.3	3	-26	-49	19
EMBIG Sovereign Spread		397	1	-14	5	-28	14
FX / Commodities / Volatility					%		
EM FX vs. USD, (+) = appreciation		46.1	-0.1	0	0	-4	-4
Dollar index, (+) = $ appreciation		101.6	0.1	-1	-3	-2	0
Brent Crude Oil ($/barrel)		77.4	0.2	-3	-6	-8	0
VIX Index (%, change in pp)		16.0	0.1	0	-1	-1	4

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

Mature Markets

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United States

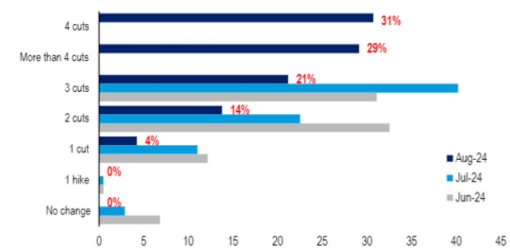
Investors overwhelmingly expect lower short term rates over the next 12 months, according to the latest survey from Bank of America. The proportion of investors expressing this view reached 93%, which is the highest in the 24-year history of the survey. A similar proportion of 94% expect the first rate cut at the September 18 FOMC meeting and 60% expect four total rate cuts over the coming year. The investor view clashes with current pricing in the short term interest rate futures market, which predicts nearly four full rate cuts by the December 18 FOMC meeting and 7.7 rate cuts by the July 30, 2025, FOMC meeting. The market thus expects a much more aggressive rate cut cycle than the investor survey. Contacts think the current market forecast is inconsistent with the widespread expectation of a soft landing. They think such a rapid pace of rate cuts would only occur if the economy was in recession, which is not the consensus forecast.

Chart 7: Expectations for lower short rates highest on record
% of FMS expecting lower short-term rates in the next 12 months

Source: BofA Global Fund Manager Survey

BofA GLOBAL RESEARCH

Chart 8: 60% of FMS expect 4 Fed rate cuts or more next 12 months
What is the most likely move for the Fed in the next 12 months?

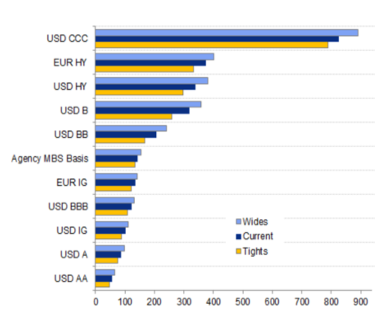


Source: BofA Global Fund Manager Survey

BofA GLOBAL RESEARCH

The US credit markets have retraced much of the credit spread widening since the July-early August selloff. Treasury yields are also off their lows, although they remain below where they were before the early Autumn selloff began. Sentiment has improved markedly since the beginning of August, and analysts point out that the credit market selloff was much less severe than the equity market selloff, as investors looked through the short term volatility to conclude that business prospects for US companies were relatively unaffected by the fallout from the Yen carry trade unwind. As the summer lull comes to an end, contacts expect a strong market for new deals in September and October as corporate issuance volumes for 2024 approach record levels. The prospect of a new Fed rate cut cycle is another potential tailwind for fixed income markets.

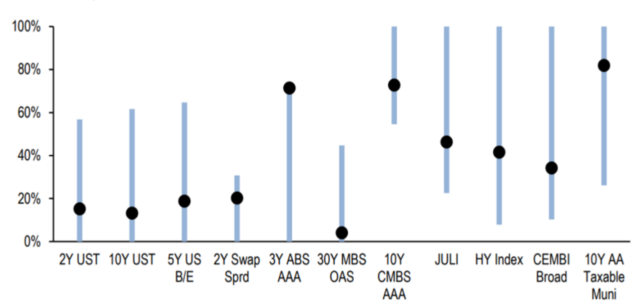
Exhibit 1: Spreads have retraced half of the late July/early August widening...
Current spreads vs. local tights and wides



	Wides	Current	Tights
USD CCC	890	824	788
EUR HY	402	374	332
USD HY	381	338	297
USD B	358	317	259
USD BB	240	205	168
Agency MBS Basis	153	141	133
EUR IG	141	135	120
USD BBB	132	121	109
USD IG	111	100	89
USD A	97	85	76
USD AA	65	56	46

Source: Bloomberg, Haver Analytics, iBoxx, Goldman Sachs Global Investment Research

Figure 1: Treasury yields have backed off their lows and credit spreads from their wides, as the relative strength in the data and risk sentiment has supported a normalization following the July payrolls report
Respective yields and spreads (black dots) within their 1-month range (blue section), normalized as a percentage of their 3-month histories; %

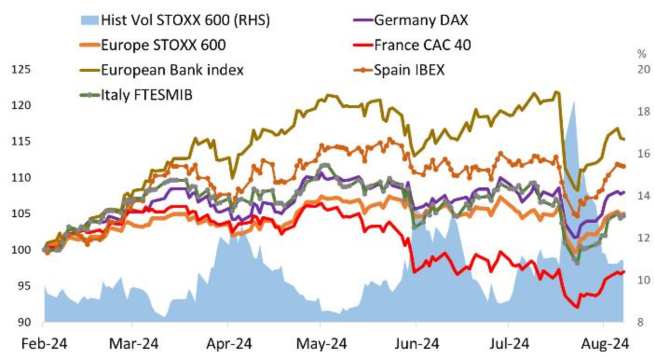


Source: J.P. Morgan

Euro Area

European equities traded higher (+0.2%) but retraced gains during the morning with the Stoxx 600 index sliding to -0.1% and stocks down in Italy and Spain. The banking sector continued to underperform the market, with Stoxx 600 Banks down -0.8% today.

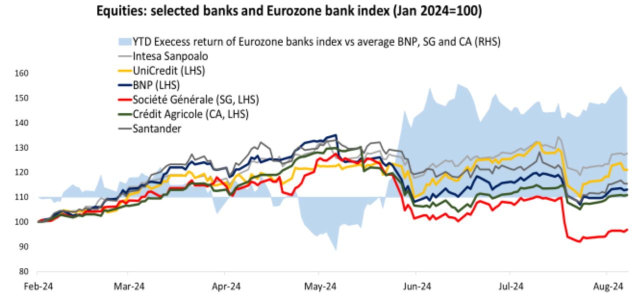
European Stocks (Jan 2023 = 100)



Source: Bloomberg and IMF calculations

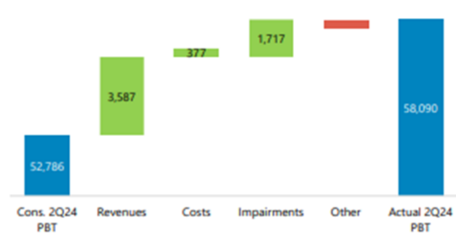
The European banking sector has lost -5.16% MTD as banks' shares were caught in the market sell-off triggered at the beginning of August by the yen carry trade unwind, weaker US job data and concerns on a possible forthcoming US recession. In last developments, losses have extended from French banks, already impacted by increased political uncertainty after the July snap elections in France, to Italian and Spanish banks (Unicredit -8% and Santander -10% on the month). Still, the Q2 2024 results of European banks showed profits in aggregate above consensus, largely due to revenue growth led by fees and commission income and lower cost of credit (loan loss provisions), although (net) interest income stagnated in absence of loan growth. Analysts at Jefferies remain constructive on Southern European (and UK) banks where they see upside from (tangible) book value per share increasing by more than 10%y/y in 2024 thanks to new share buyback programs and supporting banks' shares valuation.

Equities: selected banks and Eurozone bank index (Jan 2024=100)



Source Bloomberg and IMF calculations

European banks Q2 2024: bridge between consensus Profit Before Tax (PBT) and reported PBT, in €/m

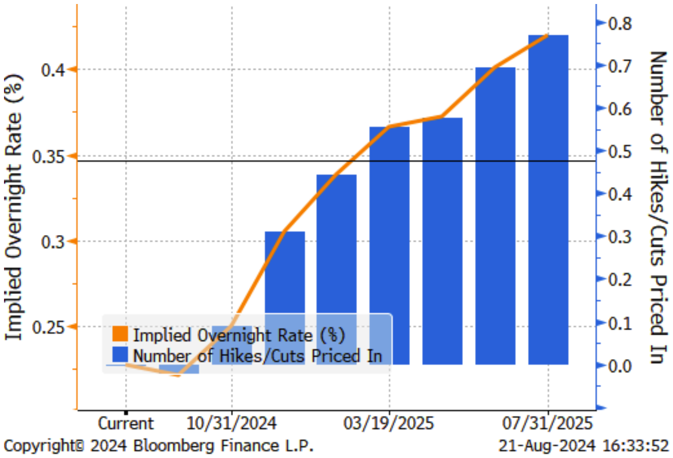


Source: Jefferies

The euro has moved above $1.11/€ against the dollar and traded this morning tightly around that level, as market participants seemed to gain confidence in a stronger euro against the backdrop of quicker Federal Reserve interest rate cuts in comparison to those for the European Central Bank. FX analysts at Blomberg highlight the potential for an inverted "head-and-shoulders pattern" which could push the euro to the $1.2/€ level in the medium-term. ING bullish on the euro; analysts noted that data released yesterday showed that the Eurozone's June's current account surplus was a monthly record at over €50bn, further supporting the rally of the euro.

Japan

Several prominent investors increased bets on stronger yen. Jupiter Asset Management's Nash reportedly has increased bets on the yen strengthening while increasing bearish bets on 10-year JGBs. He predicts the yen will rise to around 130 against the dollar with the Bank of Japan (BoJ) hikes into 2025. His views align with Vanguard, M&G and RBC BlueBay, who also foresee higher Japanese interest rates. A Reuters survey published today indicates that 57% of the economists surveyed believe the BoJ will raise interest rates again by the end of the year, contrasting with short term futures markets which are ricing in a 32% probability. Investors will keenly watching the BoJ Governor Ueda's speech at the parliament scheduled this Friday for hints about future policy.



Emerging Markets

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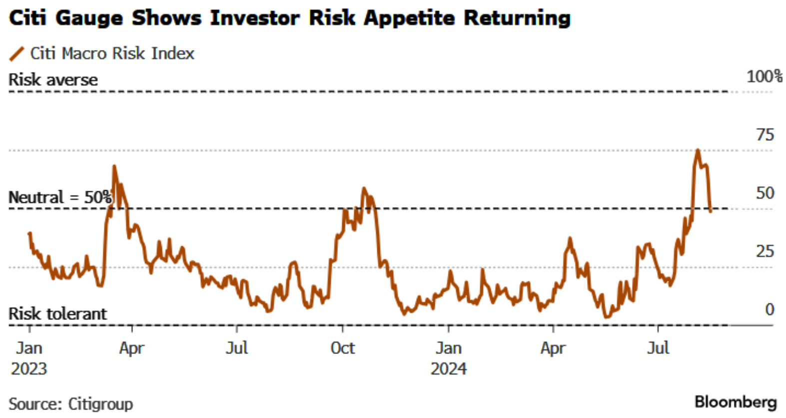
EMEA equity markets were mixed. Currencies were little changed. **Asian equities were mostly down (EM Asia: -0.9%), led by Taiwan stocks, with shares of chip makers a major drag.** Asian currencies were mixed. **Markets in Latin America were also mixed as the US equity rally stalled.** The real gave up some of its recent gains after the central bank governor pushed back against rate hike expectations.

Emerging Market FX Carry Trades

Citi analysts see hedge funds switching to the US dollar as funding currency for EM FX carry trades, in expectations of rate cuts and cheaper funding costs. The Brazilian Real and Turkish Lira were said to have benefitted from renewed carry-trade interest since Aug. 5. Citi's FX positioning indicator, which reflects its clients' positioning, shows a notable increase in bearish sentiment towards the US Dollar over the past week. In contrast, the sentiment towards EM FX is at its highest level since December 2023. Thus far in August, Citi's hedge fund clients' volumes are at the upper end of the historical range. However, Citi analyst also noted that the opportunity for these trades may be closing, as volatility and risk aversion may heighten soon due to political developments.

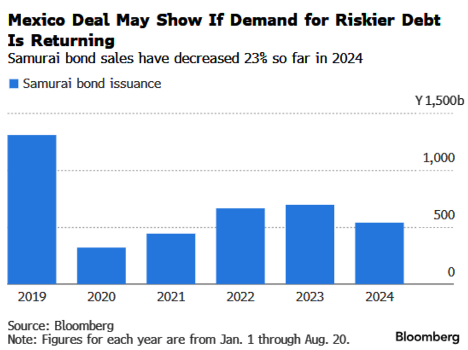


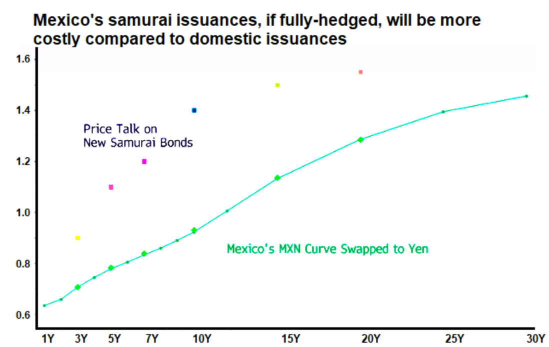
China

The Chinese regulators are concerned about the potential impact of a stronger RMB on exporters. According to a Bloomberg article, the State Administration of Foreign Exchange (SAFE) is assessing the impact of a stronger RMB on exporters, asking local state-owned lenders to survey their clients on issues such as hedging costs, currency risks, and the impact on orders and profits. Authorities are concerned about whether companies can handle the volatility and the potential impact on economic growth if the RMB continues to strengthen. **Reflecting these concerns, the RMB fixing was set weaker than market expectation for the first time in over a year.**

Mexico

Mexico is marketing a six-tranche offering of JPY notes, marking its first issuances in the samurai market in nearly two years. These notes, with maturities ranging from 3 to 20 years, may be priced later this week. The issuance will be seen as a gauge of domestic investors' appetite for riskier assets. Samurai bond sales, thus far, have declined by approximately -23% this year (*left chart*). Issuing in the samurai market provides an opportunity for EM sovereigns to diversify their investor base. While the cost of the issuance is expected to be higher on a hedged basis for Mexico (*right chart*), the funding strategy may be aimed at avoiding relying excessively on any single market and to establish on-the-run yield curves in multiple currencies.





South Africa

Rate cut expectations firmed after the July inflation print surprised on the downside. Headline inflation fell to the lowest level in three years in July (4.6% y/y versus expected 4.8% from 5.1%), and core inflation eased to 4.3% y/y (versus expectations to remain unchanged at 4.5%). Some market analysts point to the stronger rand and a decline in fuel prices as drivers for the faster-than-expected decline in inflation. The rand has strengthened by roughly 2% since the start of the month, and is now roughly 6% stronger than at the start of April, with analysts attributing the strengthening to both local pollical developments and also more recently increasing expectations that the US Federal Reserve would start cutting rates. The South African Reserve Bank has kept interest rates on hold since May 2023, with its key benchmark rate at 8.25%, and at the previous MPC meeting in July two of the six MPC members had voted for a rate cut. Market participants expect the easing cycle to begin in September.

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Global Financial Indicators

	Level		Change				
8/21/24 7:57 AM	Last 12m	Latest	1 Day	7 Days	30 Days	12 M	YTD
Equities					%		%
United States		5597	-0.2	3	2	27	17
Europe		4885	0.6	3	1	16	8
Japan		37952	-0.3	4	-4	19	13
China		3322	-0.3	0	-5	-12	-3
Asia Ex Japan		73	-0.9	2	1	14	10
Emerging Markets		43	-0.8	2	2	13	8
Interest Rates					basis points		
US 10y Yield		3.81	0.6	-2	-43	-53	-7
Germany 10y Yield		2.21	-0.3	3	-26	-49	19
Japan 10y Yield		0.88	-1.3	6	-16	23	27
UK 10y Yield		3.91	-0.1	9	-21	-82	38
Credit Spreads					basis points		
US Investment Grade		136	2.5	-5	8	-13	2
US High Yield		377	7.1	-21	25	-54	-8
Exchange Rates					%		
USD/Majors		101.56	0.1	-1	-3	-2	0
EUR/USD		1.11	-0.1	1	2	2	1
USD/JPY		146.1	0.6	-1	-7	0	4
EM/USD		46.1	-0.1	0	0	-4	-4
Commodities					%		
Brent Crude Oil ($/barrel)		77.4	0.2	-3	-5	-4	2
Industrials Metals (index)		145	0.2	5	2	4	2
Agriculture (index)		53	0.3	1	-3	-19	-14
Implied Volatility					%		
VIX Index (%, change in pp)		16.0	0.1	-0.2	-0.5	-1.1	3.5
Global FX Volatility		8.4	0.0	-0.1	1.3	-0.1	0.3
EA Sovereign Spreads					10-Year spread vs. Germany (bps)		
Greece		107	-1.0	-1	9	-23	3
Italy		137	-0.8	-1	6	-32	-31
Portugal		61	-0.8	-3	1	-12	-2
Spain		82	-0.5	-2	4	-23	-15

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

Emerging Market Financial Indicators

Last updated: 8/21/2024 8:09 AM	Exchange Rates: Level		Change (in %)					Local Currency Bond Yields (GBI EM): 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		7.13	-0.1	0.1	2	2	0		2.0	-0.6	-1	-13	-58	-55
Indonesia		15500	-0.4	1.1	5	-1	-1		6.6	-2.9	-14	-34	-1	13
India		84	-0.2	0.0	0	-1	-1		7.0	-2.0	1	-18	(73.7)	-24
Philippines		57	0.1	0.8	3	0	-2		5.1	-7.3	-2	-16	-95	-49
Thailand		34	-0.3	2.4	6	3	0		2.4	0.5	3	-21	-56	-28
Malaysia		4.38	0.1	0.9	7	6	5		3.8	-1.5	0	-5	-11	3
Argentina		944	0.0	-0.4	-2	-63	-14		39.5	-106.3	-207	-693	-6837	-4684
Brazil		5.47	0.1	0.0	2	-9	-11		11.4	11.3	6	-54	-9	102
Chile		924	-0.1	0.8	2	-6	-5		4.9	0.0	3	-35	-58	1
Colombia		4012	0.5	0.5	0	2	-3		7.7	1.5	12	-57	-60	3
Mexico		19.00	-0.1	-1.1	-6	-10	-11		8.9	-1.1	2	-51	-12	41
Peru		3.7	-0.2	-0.1	0	-1	-1		6.5	-0.2	0	-41	-66	-16
Uruguay		40	0.1	0.1	0	-6	-3		9.5	-2.2	-4	-15	29	-6
Hungary		353	0.1	1.6	1	0	-2		5.9	-6.0	7	-14	-166	15
Poland		3.86	-0.3	1.1	2	7	2		4.5	2.6	10	-46	-58	6
Romania		4.5	-0.1	0.9	2	1	1		6.5	1.1	5	-6	-23	26
Russia		91.6	-0.5	-1.9	-4	2	-2							
South Africa		17.8	-0.1	1.3	2	6	3		8.6	-12.0	5	-35	-116	-52
Türkiye		33.93	-0.1	-0.9	-3	-20	-13		28.6	-2.0	-9	65	658	188
US (DXY; 5y UST)		102	0.1	-1.0	-3	-2	0		3.69	0.2	1	-48	-78	-16

	Equity Markets: Level		Change (in %)					Bond Spreads on USD Debt (EMBIG): Level		Change (in basis points)			
	Last 12m	Latest	1 Day	7 Days	30 Days	12 M	YTD	Last 12m	Latest	7 Days	30 Days	12 M	YTD
								basis points					
China		3322	-0.3	0	-5	-12	-3		150	-5	8	-33	-8
Indonesia		7555	0.3	2	3	9	4		112	-8	7	-18	16
India		80905	0.1	2	1	24	12		110	-5	5	-29	-6
Philippines		6901	-0.6	3	3	11	7		99	-3	11	-8	19
Thailand		1338	0.7	3	2	-13	-6		0	0	0	0	0
Malaysia		1635	-0.5	1	1	13	12		90	-7	4	-8	5
Argentina		1659275	0.1	4	6	184	78		1495	-67	-95	-633	-418
Brazil		136087	0.2	3	7	19	1		228	-10	3	-11	13
Chile		6491	0.5	2	-1	6	5		125	-4	5	-3	0
Colombia		1345	-1.2	0	-2	19	13		315	-8	-1	-19	44
Mexico		53991	-0.2	1	1	2	-6		316	-6	6	-63	-18
Peru		28548	-0.5	0	-4	25	10		145	-7	3	-14	1
Hungary		73193	1.3	1	0	30	21		163	-5	13	-38	14
Poland		84238	0.6	3	-2	23	7		113	-3	13	-4	16
Romania		18348	0.2	2	-2	42	19		202	-2	14	-10	2
South Africa		84001	0.3	3	5	14	9		302	-22	0	-90	-6
Türkiye		10011	0.3	2	-10	28	34		300	-21	12	-113	-14
EM total		43	0.0	2	2	13	8		408	-16	2	24	63

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

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