



Global Markets Monitor

Monetary and Capital Markets Department
Global Markets Analysis Division

Tuesday, December 11, 2018



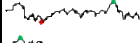





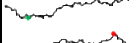

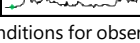
- **US equity market volatility rises and corporate bond spreads reach widest level since 2016** ([link](#))
- **Fed's Senior Financial Officer Survey suggests banks far from reserve scarcity** ([link](#))
- **French President Macron announces a series of measures addressing some of the protestors' demands** ([link](#))
- **Portugal to repay its remaining IMF debt 4 years early** ([link](#))
- **Indian assets volatile after RBI Governor Patel's surprise resignation and possible election losses facing PM Modi's party** ([link](#))

[US](#) | [Europe](#) | [Other Mature](#) | [Emerging Markets](#) | [Market Tables](#)

Constructive Signs on Trade Drive Rebound in Risk Assets

Financial markets are recovering from yesterday's widespread losses, boosted by signs of progress towards resolving trade frictions between the US and China. Bloomberg news reports that China is moving toward cutting tariffs on cars imported from the US, boosting shares of carmakers. In addition, press reports suggest that senior US and Chinese officials are coordinating on a timetable for trade talks. European and emerging market stocks are up about 2% today while US equity futures are trading almost 1% higher. On Brexit, after rescheduling today's vote in parliament, PM May is holding a series of meetings with EU leaders to discuss contentious parts of the withdrawal agreement, but counterparts have asserted that there is no scope to renegotiate. Meanwhile, French President Macron announced a number of spending measures to appease protestors. The measures would represent a considerable easing of fiscal policy, prompting a widening on France's bond spread over Germany today.

Key Global Financial Indicators

Last updated: 12/11/18 7:39 AM	Level		Change from Market Close				
	Last 12m	Latest	1 Day	7 Days	30 Days	12 M	YTD
Equities			%				%
S&P 500		2638	0.2	-4	-5	-1	-1
Eurostoxx 50		3070	1.8	-4	-5	-14	-12
Nikkei 225		21148	-0.3	-4	-5	-8	-7
MSCI EM		39	2.2	-4	-1	-15	-16
Yields and Spreads			bps				
US 10y Yield		2.89	1.3	-3	-30	50	48
Germany 10y Yield		0.27	1.9	0	-14	-3	-16
EMBIG Sovereign Spread		399	-4	4	37	110	114
FX / Commodities / Volatility			%				
EM FX vs. USD, (+) = appreciation		62.1	0.3	0	0	-9	-11
Dollar index, (+) = \$ appreciation		96.9	-0.3	0	0	5	5
Brent Crude Oil (\$/barrel)		60.5	0.8	-3	-14	-7	-10
VIX Index (% change in pp)		21.9	-0.8	1	5	13	11

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

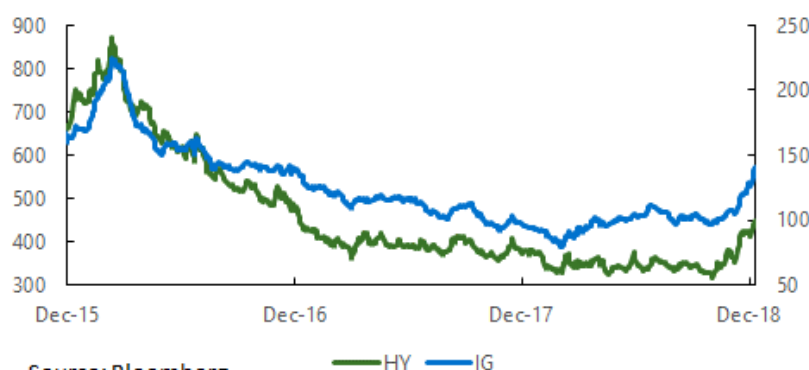
United States

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Stock markets finished in the green yesterday after a volatile session. The S&P 500 recovered from a sharp drop in the morning following the unexpected resignation of RBI governor Patel as well as the postponement of the Brexit vote by UK Prime Minister May. Technology shares contributed to the lift, while energy shares kept underperforming with lower oil prices. The VIX index of implied stock market volatility rose to 26 yesterday before easing to 22 this morning. **10-year Treasury yields were up 2 bps to 2.86%, with the yield curve flattening.** Risk-off sentiment hit credit markets hard as **both investment grade and high yield corporate bond spreads reached their highest levels since 2016.**

US Corporate Bond Spread

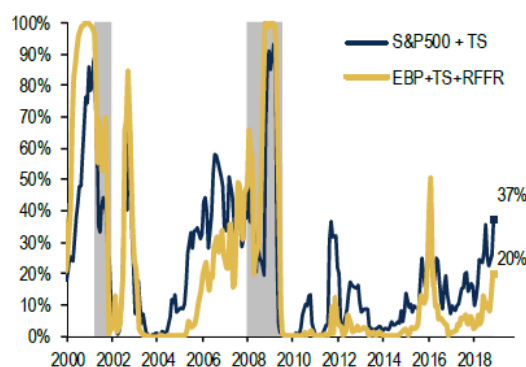
bps, versus Libor



In this morning's data, the core producer price index for November came in at 2.7% y/y (vs. 2.5% expected). The headline measure was released in line with expectations at 2.5%. The initial market reaction was muted.

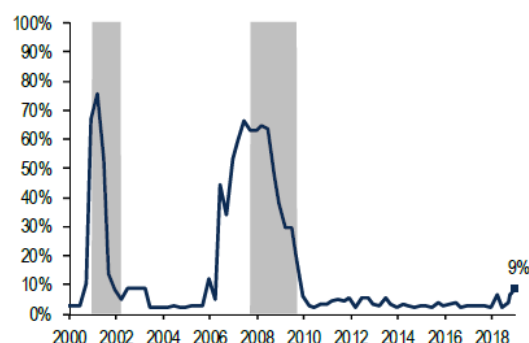
The sell-off in the stock market and the flattening of the yield curve are increasing concerns about a recession. Bank of America ML's models based on market measures show a roughly 1-in-3 chance of recession in 2019 (left chart below). Meanwhile, their model including economic variables reduces the probability to under 10% (right chart below), a low number by historic standards.

Chart 9: Probability of recession has risen (% probability of recession in next 12 months)



Note: Probit model used to estimate 12-mo ahead recession probability. S&P 500 is the 6-mo % change in the S&P 500. TS is the 3-mo 10-yr Treasury spread, EBP is the excess bond premium, and RFFR is the real fed funds rate. See [A recession indicator you don't want to miss](#) for more on the EBP. Source: BofA Merrill Lynch Global Research

Chart 10: Recession probability based on big data model suggests less near-term risk (% probability of recession in next 6 months)



Source: BofA Merrill Lynch Global Research

Fed's Senior Financial Officer Survey hints banks are far from reserve scarcity. The Fed released the results to the survey with the November FOMC minutes last week, which collected information from 51 banks regarding their reserve balance management strategies and practices. According to the results, the lowest comfortable levels of reserve balances by all respondent banks is about \$600 bn as of August 2018. Total reserve balances among respondents were about \$1.4 tn, suggesting that banks are far from an environment where reserves are scarce. The manner in which banks plan to refill their reserves varies between domestic banks and foreign banks. Most domestic banks would increase their Federal Home Loan Bank (FHLB) advance borrowing should they find themselves short in reserves. In contrast, most foreign banks would tap the unsecured funding markets, increase their wholesale deposit rates, and/or reduce their lending in repo markets. Analysts point out that if we see FHLB advance borrowing increase materially or if there is a sustained widening in the gap between money market rates and OIS this would indicate an insufficient amount of reserves in the banking system, all else equal.

1. Given the constellation of short-term interest rates relative to the interest on excess reserves (IOER) rate over the past month, what is the approximate lowest dollar level of reserve balances that your bank would be comfortable holding before it began taking active steps to maintain or increase its reserve balance position?⁵

	All Respondents	Domestic	Foreign
Totals	(billions of dollars)		
Reported lowest comfortable level of reserve balances	617.2	385.0	232.2
Average reserve balances in August 2018 *	1,368.2	827.5	540.7

* Federal Reserve data.

Source: FRB

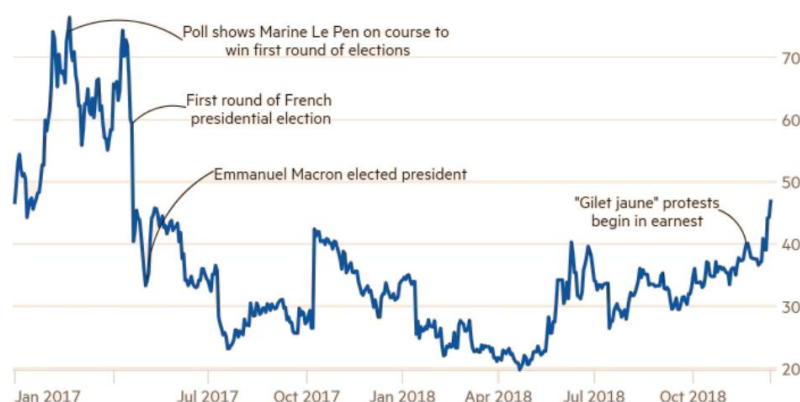
Europe

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The EuroStoxx 600 is up 1.5%, nearly offsetting yesterday's 1.8% drop. Stocks in Germany and France are leading the rebound. **Fixed income markets are mixed in narrow ranges across the region.** Of note, yields are rising in France and Italy, around 4 bps across the curve. The spread between 10-year French bonds and German bunds has risen to 46 bps, the highest since the blowout during the 2017 elections, and twice as high as the low for the year seen in April.

France's 'le spread' at highest level since 2017 elections

France 10-year yield spread over German bunds (basis points)



Source: Refinitiv

France

President Macron delivered a *mea culpa* and announced a series of measures addressing some of the protestors' demands. Measures include a subsidized minimum wage increase by €100 per month (i.e. the employer would not bear the cost), removal of taxation on overtime and bonuses, and cancellation of taxes for pensions below €2000. He did not retreat on cutting the wealth tax. Some estimates place the cost of the measures at €11 bn, taking the 2019 deficit well over the stability pact threshold of 3.0% to around 3.5%.

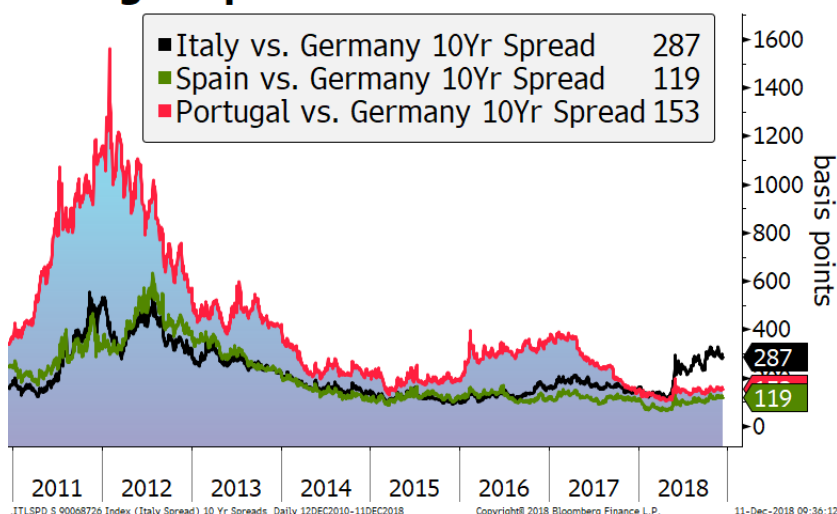
United Kingdom

The pound recovered somewhat from its sharp drop yesterday after PM May delayed the Brexit vote that had been scheduled for today. She has given no guidance on a new date for the vote but signaled the need to step up preparations for a no-deal Brexit. The Irish backstop is still the most contentious issue preventing her from gaining support in parliament. May will now meet with EU leaders to discuss the concerns ahead of a summit meeting in Brussels on Thursday. EC President Tusk reinforced the line that the EU "will not renegotiate the deal, including the backstop," but said they are "ready to discuss how to facilitate UK ratification." On net, sterling has depreciated about 1% over the last two sessions, while the FTSE 100 is up slightly and longer-dated yields are down some 3 bps over the same period.

Portugal

The government will repay its remaining €4.7 bn debt with the IMF debt 4 years earlier than expected. The decision will lead to savings of about €100 mn in interest payments and relieve the financing needs in 2021 and 2022. Officials made the decision considering the current environment of extremely low interest rates, favorable borrowing conditions for the sovereign, and the sound state of Portugal's public finances. For reference, Portugal's spread to equivalent 10-year German bunds is now around 150 bps, well below its 5-year average of 230 bps and the 2017 high of 390 bps.

Portugal Spread



Other Mature Markets

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Japan

The yen gained against the dollar (+0.2%) amid limited risk appetite while equities lost ground. The Topix (-0.9%) fell to its lowest level since last May as electronics and machinery makers dragged the composite lower, while telecommunications shares rose. **JGB yields rose 0.5 to 1.2 bps across the curve**

following a poorly-received bond auction. The sale of the 30-year long bond drew limited demand. The auction received a bid-to-cover ratio of 3.78x, its lowest in nearly a year. This auction marked the first sale of super-long bonds since the BoJ reduced the number of days on which it would buy bonds maturing in more than 25 years from 5 previously to 4 for December.

Emerging Markets

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Asian equities were mixed today but the MSCI Asia ex Japan index extended recent declines to end the day 0.4% lower. By Bloomberg's estimate, Asian equities have lost more than \$1 tn in market value since December 3 and are now trading at a six-week low. **Asian currencies were also mixed**, with the Indian rupee (-0.7%) underperforming on the back of central bank governor Patel's surprise resignation. The RMB, by contrast, was supported by the latest signs of dialogue between the US and China and outperformed its Asian peers; both the onshore and offshore RMB gained 0.1% on the day. **In EMEA, major equity indices are mostly little changed**, with the notable exception of South Africa (+1.0%). Regional currencies are slightly stronger on the day, but the Turkish lira is underperforming (-0.5%) despite the robust current account data release. **Latin American** assets were broadly lower yesterday on US-China trade tensions and slowing global growth concerns. Argentine and Brazilian equities both declined by 2.5%, continuing their downward trend this week and reversing any gains seen earlier this month. Mexico, Chile and Colombia's benchmark indices were down more than 1%. The Argentine peso and Brazilian real weakened by 0.8% and 0.4% against dollar, respectively.

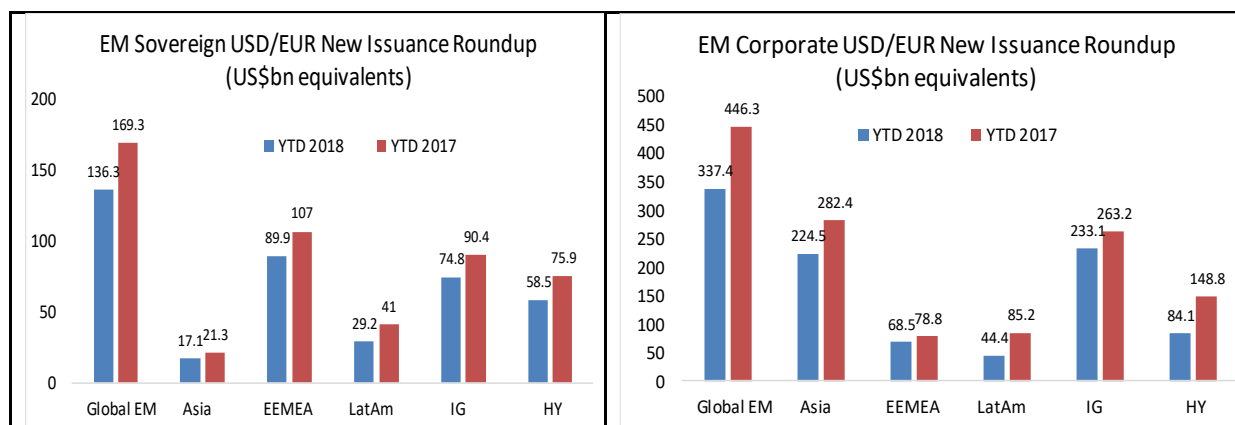
Key Emerging Market Financial Indicators

Last updated: 12/11/18 7:52 AM	Level		Change				YTD
	Last 12m	index	1 Day	7 Days	30 Days	12 M	
Major EM Benchmarks			%				%
MSCI EM Equities		39.46	2.1	-4	-1	-15	-16
MSCI Frontier Equities		27.41	-0.9	-1	0	-18	-17
EMBIG Sovereign Spread (in bps)		398	-5	3	36	109	113
EM FX vs. USD		62.04	0.2	-1	0	-9	-11
Major EM FX vs. USD			%, (+) = EM currency appreciation				
China Renminbi		6.90	0.2	-1	1	-4	-6
Indonesian Rupiah		14608	-0.4	-2	1	-7	-7
Indian Rupee		71.86	-0.7	-2	1	-10	-11
Argentine Peso		37.68	-0.8	-3	-6	-54	-51
Brazil Real		3.90	0.5	-1	-4	-15	-15
Mexican Peso		20.24	0.4	1	1	-6	-3
Russian Ruble		66.35	0.5	1	2	-11	-13
South African Rand		14.30	0.6	-3	1	-5	-13
Turkish Lira		5.37	-0.8	0	2	-29	-29
EM FX volatility		10.19	0.0	0.3	0.2	2.3	2.3

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

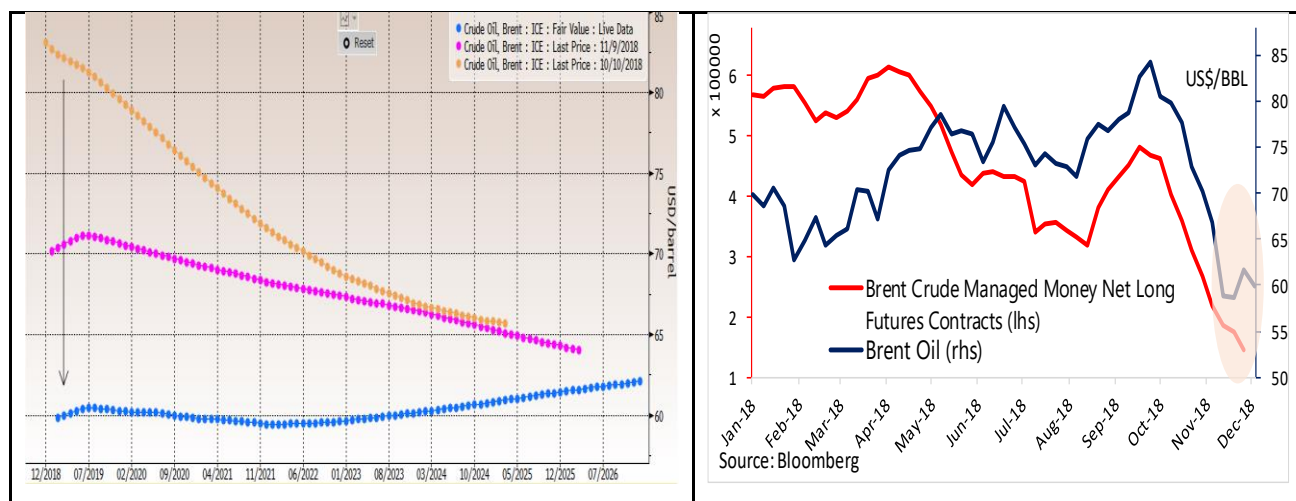
EM bond issuance remained subdued last week at \$8.2 bn, slightly lower than the week before.

Indonesia was the only country to issue sovereign bonds (worth \$3 bn), rated investment grade, and while China was the only major issuer of corporate bonds, valued at \$5.1 bn, of which \$4.5 bn were investment grade. The total YTD bond issuance of \$473 bn is approximately 23% less than the 2017 issuance over the same period.



Source: Bloomberg

Oil prices weakened significantly yesterday despite the agreed production cuts amongst OPEC+ countries last Friday. Participants seemed to doubt the effective implementation of these production cuts, which contributed to the 3% decline in the Brent price. The front end of the oil futures curve continued to be weighed down by concerns about excess supply in the short-term, as evidenced by the sharp drop in the price of short-dated contracts since early October. Analysts also observed that speculators continued to reduce their net-long futures positions, adding further downward pressures on oil prices. It is notable that the long-end of the futures curves continues to be anchored at around \$60-\$65/barrel, reflecting market views of future equilibrium oil prices.



India

Indian assets endured a volatile session following RBI Governor Patel's surprise resignation as well as the possible election losses facing PM Modi's party. The Governor resigned late on Monday, citing personal reasons. Meanwhile, exit polls suggest that PM Modi's party faces a tight contest and could lose power in at least three major states. The rupee lost as much as 1.6% intraday before settling at 71.81/USD (-0.7%). Bonds also saw a volatile session. The 10-year yield surged as much as 13 bps to 7.71% intraday, its highest since late November before ending the day 5 bps lower at 7.54%. The 1- and 3-year notes ended the day little changed. On a more positive note, the S&P BSE Sensex Composite erased initial losses of as much as 0.7% to end the day 0.5% higher.

Turkey

The current account saw a record surplus in October of \$2.8 bn, slightly higher than expected. This compares to a \$3.8 bn deficit in October 2017. The slowdown in domestic demand and a favorable export performance were the main drivers. Exports rose 10.4% yoy compared to a 23.8% yoy decline in imports. Analysts think the rebalancing of the Turkish economy is likely to continue at least through the first half of 2019, which should serve as an important source of medium-term support for the lira, even though the currency did not seem to benefit from the news today.

Current account (USD bn)



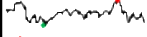

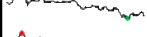

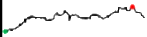




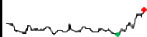










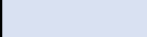



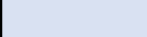


Source | CBT



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Global Financial Indicators

Last updated: 12/11/18 7:39 AM	Level		Change				YTD
	Last 12m	Latest	1 Day	7 Days	30 Days	12 M	
Equities			%				%
United States		2638	0.2	-4	-5	-1	-1
Europe		3070	1.8	-4	-5	-14	-12
Japan		21148	-0.3	-4	-5	-8	-7
China		2594	0.4	-3	0	-22	-22
Asia Ex Japan		64	-0.7	-4	1	-15	-16
Emerging Markets		39	2.2	-4	-1	-15	-16
Interest Rates			basis points				
US 10y Yield		2.89	1.3	-3	-30	50	48
Germany 10y Yield		0.27	1.9	0	-14	-3	-16
Japan 10y Yield		0.05	0.7	-2	-7	0	0
UK 10y Yield		1.23	2.9	-5	-26	3	4
Credit Spreads			basis points				
US Investment Grade		140	2.2	14	34	45	49
US High Yield		447	6.5	35	83	68	72
Europe IG		85	-2.7	3	13	38	40
Europe HY		344	-11.1	16	50	113	111
EMBIG Sovereign Spread		399	-4.0	4	37	110	114
Exchange Rates			%				
Dollar Index (DXY)		96.92	-0.3	0	0	3	5
USDEUR		1.14	0.3	0	2	-3	-5
USDJPY		113.1	0.2	0	1	0	0
EM FX vs. USD		62.1	0.3	0	0	-9	-11
Commodities			%				
Brent Crude Oil (\$/barrel)		60	0.8	-3	-14	-7	-10
Industrials Metals (index)		115	1.1	-1	0	-9	-17
Agriculture (index)		43	0.1	0	1	-8	-9
Implied Volatility			%				
VIX Index (% change in pp)		21.9	-0.8	1.1	4.5	12.5	10.8
10y Treasury Volatility Index		4.4	0.0	0.6	0.6	0.7	0.9
Global FX Volatility		8.7	0.0	0.3	0.5	1.3	1.4
EA Sovereign Spreads			10-Year spread vs. Germany (bps)				
Greece		400	-1.1	2	2	-23	31
Italy		287	0.8	-3	-13	151	128
Portugal		152	-2.1	-3	-2	1	0
Spain		119	-0.6	-3	0	7	5

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: 12/11/2018 7:52 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		6.90	0.2	-0.9	1	-4	-6		3.2	-2.1	-10	-24	-75	-75
Indonesia		14608	-0.4	-2.2	1	-7	-7		8.4	16.9	32	8	157	174
India		72	-0.7	-1.9	1	-10	-11		7.6	8.6	-6	-22	33	15
Philippines		53	0.0	-0.5	1	-5	-5		6.3	-0.3	-5	-43	146	143
Thailand		33	0.0	-0.3	1	0	-1		2.7	0.0	-7	-18	37	41
Malaysia		4.18	-0.3	-0.9	0	-3	-3		4.1	-0.3	-4	-2	17	22
Argentina		38	-0.8	-3.1	-6	-54	-51		23.2	7.0	29	-48	744	722
Brazil		3.90	0.5	-1.4	-4	-15	-15		8.6	7.7	7	-17	-27	-40
Chile		679	0.2	-1.6	1	-3	-9		4.6	0.8	-4	-22	-32	-19
Colombia		3190	-1.1	0.2	0	-6	-6		6.6	-1.4	-7	-20	31	36
Mexico		20.24	0.4	1.4	1	-6	-3		9.2	2.4	1	27	181	149
Peru		3.4	0.0	0.4	0	-4	-4		5.9	4.8	12	5	61	66
Uruguay		32	-0.2	-0.8	1	-10	-11		11.0	0.7	21	37		245
Hungary		284	0.2	0.4	1	-6	-9		2.3	0.9	-1	-40	102	108
Poland		3.78	0.1	-0.1	2	-6	-8		2.4	-2.4	-2	-14	-23	-25
Romania		4.1	0.1	0.3	1	-4	-5		4.2	-1.0	-7	-16	35	33
Russia		66.3	0.5	0.7	2	-11	-13		8.4	0.6	6	-23	104	112
South Africa		14.3	0.6	-3.1	1	-5	-13		9.9	16.9	31	9	2	54
Turkey		5.37	-0.8	0.4	2	-29	-29		17.7	15.7	92	11	546	579
US (DXY; 5y UST)		97	-0.3	0.0	0	3	5		2.75	3.2	-4	-29	59	54

	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		2594	0.4	-3	0	-22	-22		188	-4	-3	4	40	36
Indonesia		6077	-0.6	-1	3	1	-4		230	-3	3	19	60	64
India		35150	0.5	-3	0	5	3		180	-3	2	11	70	70
Philippines		7451	1.4	-3	7	-11	-13		114	-3	-1	11	18	19
Malaysia		1653	-1	-2	-3	-4	-8		148	-4	-3	12	37	38
Argentina		30754	-2.5	-4	3	13	2		746	-7	17	131	381	396
Brazil		87075	-2.5	-2	2	20	14		268	-4	-2	18	35	34
Chile		5036	-1.2	-2	-3	0	-10		161	-4	-3	21	42	42
Colombia		1377	-0.4	-2	-3	-6	-9		205	-3	-8	13	29	31
Mexico		41356	-1.2	-2	-7	-13	-16		343	-4	-3	38	97	98
Peru		19202	-1	-1	1	0	-4		169	-3	-2	15	34	32
Hungary		39785	1.4	-3	3	6	1		149	-3	0	27	62	61
Poland		57725	0.6	-3	1	-7	-9		71	-7	-6	15	32	24
Romania		8584	0.3	-2	-1	13	11		228	1	12	42	111	114
Russia		2402	-1.2	-2	0	12	14		244	-6	0	14	62	66
South Africa		51106	1.3	-2	-4	-12	-14		359	-8	4	32	82	105
Turkey		92265	0.0	-2	-1	-15	-20		464	-15	0	40	164	175
Ukraine		574	-0.3	0	-4	89	82		743	3	30	130	275	288
EM total		24	0.0	-3	0	-11	-11		398	-5	3	36	109	113

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