GLOBAL MARKETS ANALYSIS
Monetary and Capital Markets

Global Markets Monitor

FRIDAY, DECEMBER 18, 2020

- **US HY bond issuance strong in December; fallen angel bonds improve HY credit quality** (link)
- **Germany's IFO survey confirms business resilience** (link)
- **European banks' LCRs rise sharply in Q2 driven by increasing central bank reserves** (link)
- **BoJ maintains policy stance; will conduct assessment for further monetary easing** (link)
- **Australian bank regulator posts reassuring stress test results; cancels dividend limits** (link)
- **Asian markets weighed down by news US could blacklist more Chinese companies** (link)
- **Central Bank of Russia leaves policy rate unchanged, as expected** (link)
- **Banxico holds policy rate steady; reinforces data dependency going forward** (link)

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

Markets trade cautiously as investors await more clarity on the political front

Global risk assets are mixed this morning as the wait for a deal both in the US and between the UK and EU continues. In the UK, while the overall tone is still cautiously optimistic that a deal will be struck, the sticking point of fishing rights persists, which has paused the recent UK pound appreciation this morning. The EU Parliament has been reported to have set Sunday as the new deadline for the talks, while European stocks are holding steady this morning with modest gains following some slightly better than expected data releases. In the US, yesterday the S&P 500 rose (+0.6%) to a new all-time high with markets seemingly optimistic that somewhat weaker data and the upcoming US government shutdown deadline will motivate Congressional leaders to reach a compromise on economic relief. In light of the positive risk sentiment, US Treasury yields moved slightly higher led by rising breakeven inflation rates, while the US dollar depreciation accelerated (-0.7%) before showing signs of stabilizing this morning. The weaker dollar kept commodity prices on the upswing with front-month Brent oil prices now above $51 a barrel, the highest level since early-March. In addition, news that the US is looking to blacklist dozens of Chinese firms weighed on Asian markets overnight with most regional equity indices closing with losses.

Key Global Financial Indicators

Last updated: 12/18/20 8:08 AM	Level: Last 12m	Level: Latest	Change from Market Close: 1 Day	7 Days	30 Days	12 M	YTD
Equities					%		%
S&P 500		3722	0.6	1	4	17	15
Eurostoxx 50		3566	0.2	2	2	-5	-5
Nikkei 225		26763	-0.2	0	4	12	13
MSCI EM		51	0.7	0	5	15	14
Yields and Spreads					bps		
US 10y Yield		0.93	-0.7	3	6	-99	-99
Germany 10y Yield		-0.57	0.2	7	-1	-32	-38
EMBIG Sovereign Spread		353	-4	-11	-26	60	64
FX / Commodities / Volatility					%		
EM FX vs. USD, (+) = appreciation		57.9	0.0	1	3	-5	-6
Dollar index, (+) = $ appreciation		89.9	0.1	-1	-3	-8	-7
Brent Crude Oil ($/barrel)		51.3	-0.3	3	16	-22	-22
VIX Index (%, change in pp)		21.9	0.0	-1	-2	9	8

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

United States

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U.S. stocks rallied and closed up 0.6%, even as lawmakers continue to wrangle over the proposed federal-spending deal. Commentary from the Fed on Wednesday was perceived as slightly dovish, which offset the concerns over an unexpectedly large rise in the US jobless claims yesterday. Treasury yields continued to widen as the risk-on mode gained further momentum. A key investor focus was the persistent pressure on the US dollar, which depreciated by 0.7% today extending the depreciation over the last month to more than 3% (dropping to a fresh 2.5 year low).

The US dollar has depreciated by more than 4% since the end of October (and by 12% since of the peak of the sell-off in March), with this remaining a key area of focus for investors. Analysts note that a significant fiscal boost, supportive Fed policies in terms of continued asset purchases, and a global risk-on sentiment (driven by the vaccine optimism) are likely to weigh on the USD dollar. However, market contacts also highlight that there is now stretched positioning, which may have already overshot a broad-based dollar depreciation.

Dollar at Multi-year Lows

Source: Bloomberg

S&P LCD data shows that December's high-yield bond issuance is on track to exceed $29 bn through Friday, pushing above the prior December peak of $27.6 bn, in 2012. After three consecutive years of decline, the face amount of outstanding high-yield bonds has rebounded to a new all-time high. With just two weeks left in the year, new-issue volume has already crossed the previous record by more than 25%. As of Dec. 17, the week was slated to wrap with roughly $11 bn cleared in the primary market, advancing year-to-date volume to almost $435 bn.

Change in face amount outstanding ($B)

	HY index	Original issues	Fallen angels	Total
12/31/2016	1,298	1,133	165	
12/31/2019	1,214	1,104	110	
Change	-84	-29	-55	-84
% of change		34.5	65.5	100.0

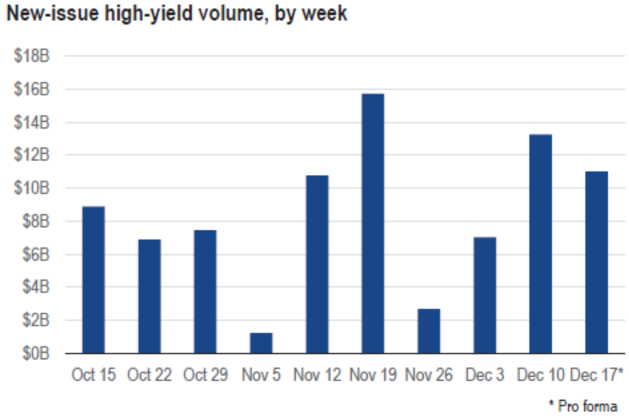
Source: ICE Indices, LLC

Change in face amount outstanding ($B)

	HY index	Original issues	Fallen angels	Total
12/31/2019	1,214	1,104	110	
11/20/2020	1,433	1,201	232	
Change	+219	+97	+122	+219
% of change		44.3	55.7	100.0

Source: ICE Indices, LLC

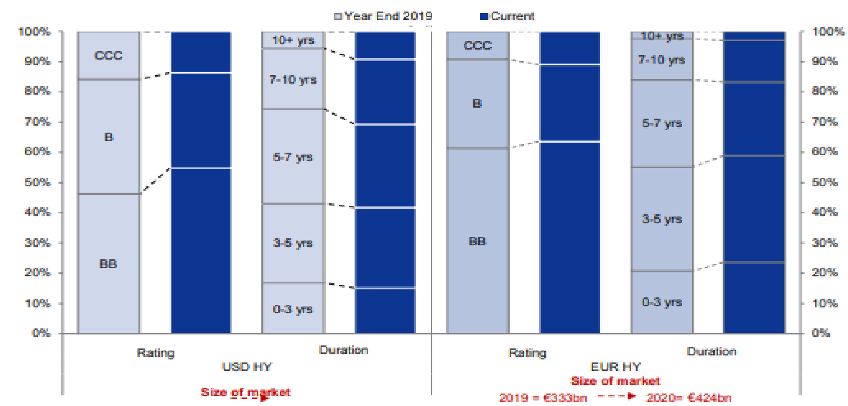
New-issue high-yield volume, by week



Source: LCD, an offering of S&P Global Market Intelligence

Along with the turnaround in the high-yield market issuance, 2020 is noteworthy for a significant change in the composition of the market as well. Goldman analysts highlight that driven in part by a wave of fallen angels, the average quality has improved, with the share of BB-rated bonds increasing from 46% of the index to 55%. The market's average duration moved higher as fallen angels increased the share of long-dated bonds. Analysts also note that the same trend prevailed in the EUR HY market in terms of size and quality. The market grew by 27%, to €424 bn of total face value from €333 bn in 2019. BB-rated bonds also grew their share to 64% from 61% in year-end 2019. But in contrast to the USD HY market, the duration composition of the EUR HY universe has moved in the opposite direction, the share of short-dated bonds increasing to 24% from 21%, while the share of long-dated bonds declined to 24% from 29%, over the same period.

Exhibit 12: The share of BB-rated and longer dated bonds in the USD HY market has increased
Notional breakdown of the USD and EUR HY market at YE 2019 vs. today



Source: Bloomberg, Goldman Sachs Global Investment Research

Europe

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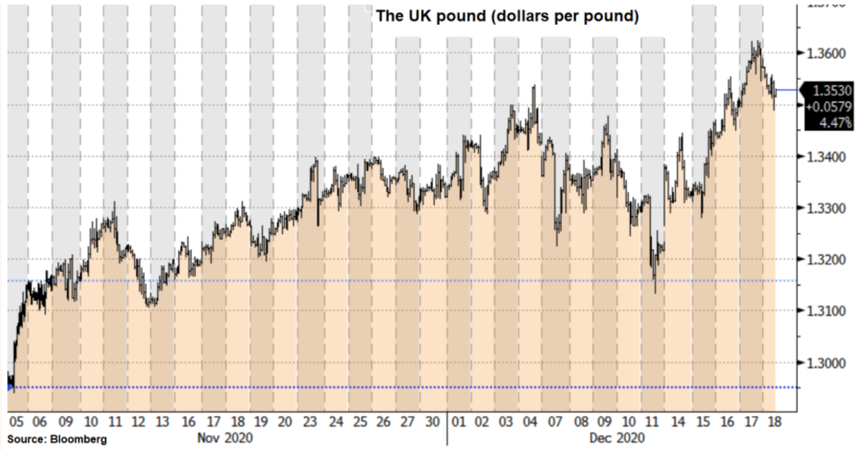
European equities were mostly trading sideways around the post-pandemic highs. While European equities have recovered substantially since March, the year-to-date performance remains behind major global peers even when considering the euro valuation gains.

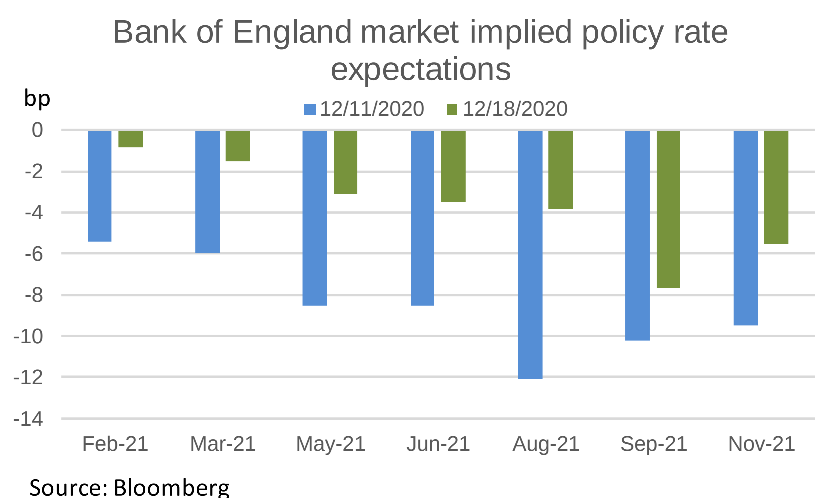
Source: Bloomberg

European bond yields were drifting higher with 10-year bund yields up 1 bp and Southern European spreads 1-2 bps wider.

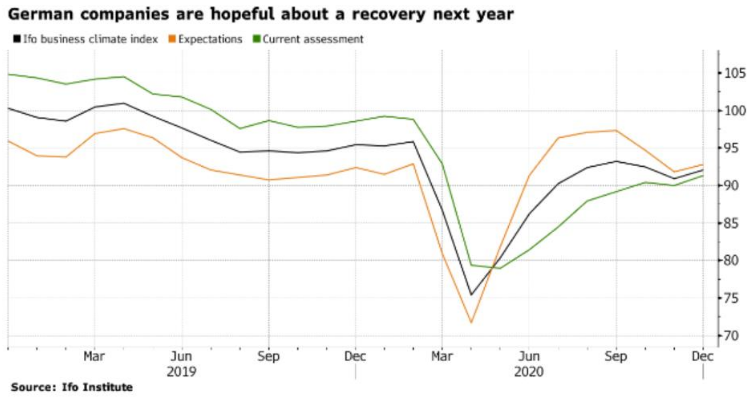
The euro (-0.1%) was little changed while the pound (-0.5%) gave up some of yesterday's gains with contacts reporting profit taking as markets move into low liquidity phase over the next two weeks. While this upcoming Sunday was named as another deadline, it seems that negotiations could drag on until the very last moment as diplomats send conflicting messages regarding the negotiation progress.



Following the Bank of England (BOE) decision to keep its stimulus unchanged, most analysts noted the cautiously optimistic tone of the meeting minutes amid generally elevated uncertainty due to ongoing trade negotiations. Unless the trade talks end with no deal, most analysts now expect the BOE to keep its current monetary policy setting for the foreseeable future. That said, some contacts argue that the central bank may need to increase the QE envelope by another £100-150 bn given the potential pressure on the yield curve from increased bond supply as the existing asset purchases envelope will not last until the end of 2021 should the purchases continue at current pace (£4 bn per week). In terms of negative rates, **over the last week markets have significantly scaled back rate cut expectations with most contacts seeing further cuts only in a no-deal scenario**. Separately, the UK Chancellor Sunak extended the current furlough scheme by an extra month until the end of April 2021.

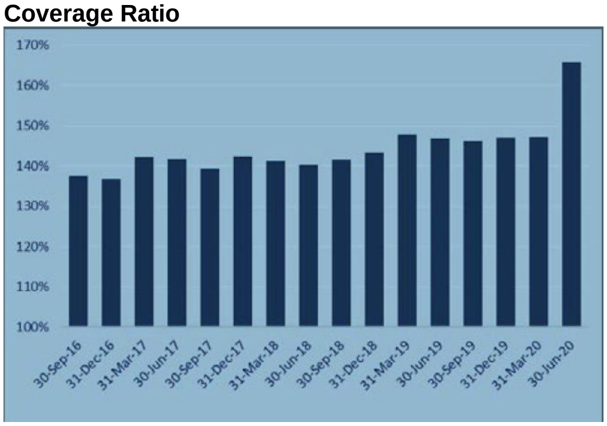


Germany IFO business survey showed remarkable resilience in December. Contrary to market consensus estimates, the current assessment and expectations readings increased despite stricter containment measures. As with the PMI readings, sentiment in the manufacturing sector gained momentum while the service sector saw some recovery in business expectations. That said, the survey was carried out before the tighter nation-wide restrictions were imposed on the 16th of December. Most businesses expect curbs to be lifted by July 2021.

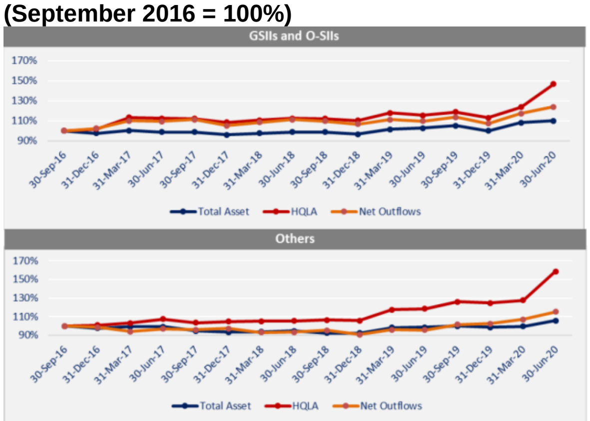


European banks' LCRs rose sharply in 2Q2020, facilitated by the expansion of central bank reserves. The European Banking Authority's quarterly review across the 117 banks it supervises shows liquidity coverage ratios (LCRs) rose to 166% at the end of 2Q2020, up nearly 20 percentage points from the previous quarter. No bank in the sample reported an LCR below the 100% regulatory minimum. The positive recent trend --consistent across banks of varying size, systemic importance and business models -- was driven mainly by banks' massive accumulation of 'high quality liquid assets', primarily an increase of central bank reserves from about 6% to nearly 10% of bank assets on average. This quantifies the degree to which banks, at least through mid-2020, averted the feared impact of the COVID-19 shock on bank liquidity positions.

European Banks: Weighted Average Liquidity Coverage Ratio



Growth of HQLA, Net Outflows and Assets (September 2016 = 100%)



Source: European Banking Authority

Other Mature Markets

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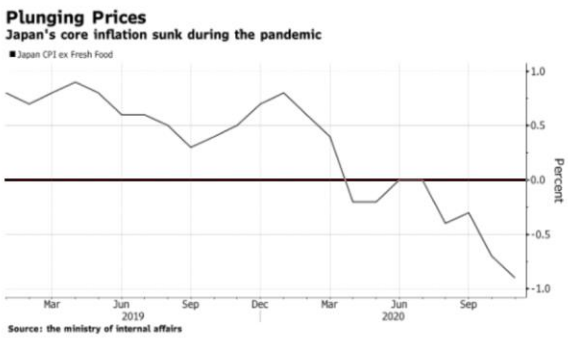
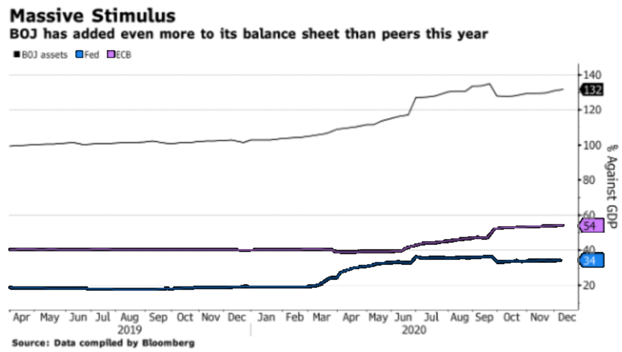
Japan

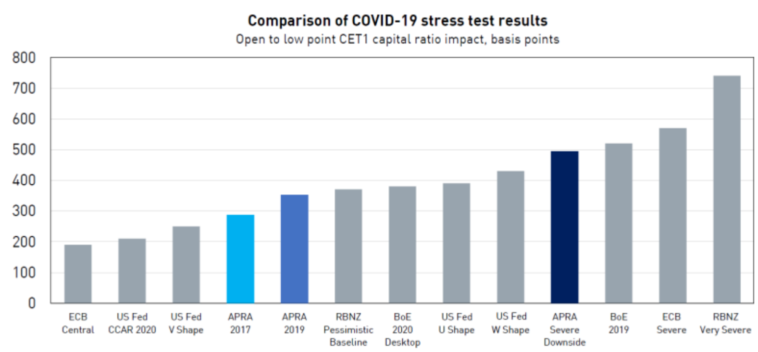
Bank of Japan (BoJ) extended its special funding programs for virus-hit businesses while keeping its key interest rates and asset purchases unchanged, as expected. The duration of the special program was extended by six months until end-September 2021. The BoJ judged that there was no need to change the framework of QQE with yield curve control, however, it pledged to assess sustainability of easing policy and to make public its findings likely at the March 2021 meeting. The decision came after the November CPI release. The fall in consumer prices deepened with both Japan's national CPI and price index excluding fresh food dropping 0.9% y/y last month. Separately, **Japan is considering a record budget for next fiscal yea**r. Government spending may increase to ¥106.6 tn ($1 tn) in the year starting April, according to Bloomberg. The official announcement of the budget figures is expected next week. **Equities were flat, the yen depreciated -0.2% and 10-year JGB yield was unchanged.**

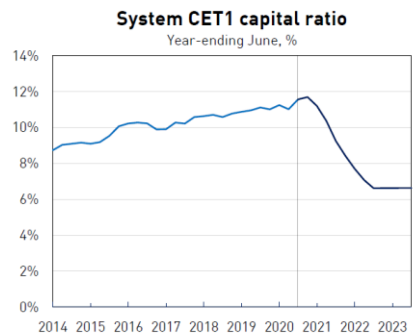




Australia

Australia's bank supervisor issues reassuring stress test results and cancels dividend restrictions. The Australian Prudential Regulation Authority's (APRA) updated stress test suggested a decline in risks to bank solvency. Despite improvement in the macro environment, APRA's severely adverse macro scenario remains conservative: 15% contraction in GDP during 2020, unemployment to 13%, 40% decline in commercial real estate prices, and an assumption that banks continue lending through the downturn. Under this scenario, the system-wide CET1 ratio declines by about 500 bps – fairly severe compared with stress tests in other jurisdictions. While banks would under this scenario be compelled to dip into available buffers (which APRA has consistently stressed are available for use), they would remain well above the regulatory minimum 4.5% CET1 ratio. Partly based on these reassuring results, APRA has cancelled the guidance, introduced in July, limiting bank dividend payouts to no more than 50% of earnings.





Source: APRA

Emerging Markets

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Latin American equity markets were mostly higher on Thursday. Chile outperformed as the equity index went up 2.2%, followed by Colombia (+1.6%) and Mexico (+1.2%), while the Argentine equity index slightly declined. **Local currencies were generally stronger.** The Chilean peso was the best performer, appreciating 1.6% against the dollar, followed by the Brazilian real (+0.4%). 10-year government bond yields dropped 7 bps in Mexico and were generally lower in other countries. **Asian equities fell -0.5% on broad-based losses.** Malaysia underperformed (-1.3%), China and Hong Kong slipped on expectations of more Chinese companies to be blacklisted by the US (Shanghai -0.3%; Shenzhen -0.3%, Hang Seng -0.7%). **Regional currencies were little changed, Thai baht outperformed (+0.2%), Korean won depreciated (-0.6%). Equities across EMEA were mixed again**, as investors struggle to find firm themes towards the year end. By country, Kuwait (+1.2%), Turkey (+0.5%), and UAE (+0.4%) posted the largest gains. Poland (-0.7%), Egypt (-1.3%), and South Africa (-0.7%) saw the largest losses in the region. In FX markets, currencies mostly depreciated against the dollar, with the largest move seen in the Russian ruble (-1.3%) and the Hungarian forint (-0.5%).

Key Emerging Market Financial Indicators

Last updated:	Level		Change				
12/18/20 8:12 AM	Last 12m	index	1 Day	7 Days	30 Days	12 M	YTD
Major EM Benchmarks			%				%
MSCI EM Equities		51.05	0.0	0	5	15	14
MSCI Frontier Equities		28.44	-0.4	2	3	-5	-6
EMBIG Sovereign Spread (in bps)		353	-4	-11	-26	60	64
EM FX vs. USD		57.89	0.0	1	3	-5	-6
Major EM FX vs. USD			%, (+) = EM currency appreciation				
China Renminbi		6.54	-0.1	0	0	7	6
Indonesian Rupiah		14110	0.0	0	0	-1	-2
Indian Rupee		73.57	0.0	0	1	-4	-3
Argentine Peso		82.84	-0.1	-1	-3	-28	-28
Brazil Real		5.11	-0.8	-1	5	-20	-21
Mexican Peso		19.85	-0.2	1	2	-4	-5
Russian Ruble		73.55	-0.9	-1	3	-15	-16
South African Rand		14.57	0.5	4	6	-2	-4
Turkish Lira		7.66	0.5	2	1	-23	-22
EM FX volatility		10.28	0.0	0.0	-0.1	3.8	3.7

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

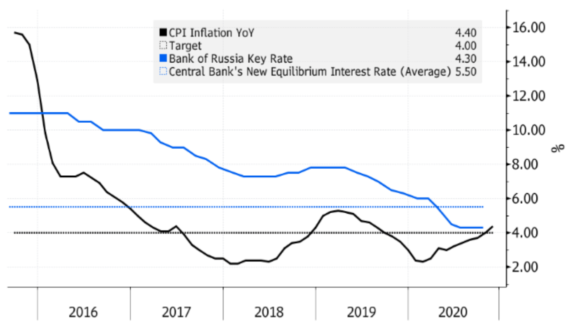
China

The US is set to add dozens of Chinese companies to a trade blacklist on Friday, according to Reuters. The list will allegedly include the country's top chipmaker SMIC. In total, the US may add around 80 additional companies and affiliates to the so-called Commerce Department's Entity List. The list already has over 275 China-based firms and affiliates, including Huawei Technologies Co., and denies access to U.S. technology from software to circuitry. Separately, **China's money market rates rose for a second day after PBoC refrained from adding extra funds to the financial system**. The overnight repo rate increased 35 basis points to 1.71%, set for the highest since Nov. 24. The benchmark seven-day repo rate rose 22 basis points to 2.11%. **The RMB depreciated (-0.12% onshore; -0.15% offshore) and equities fell (Shanghai -0.3%; Shenzhen -0.3%).**

Russia

The Central Bank of Russia kept interest rates at 4.25%, as expected. The move came even as inflation inched out of the central bank's target band. Headline CPI inflation had reached 4.4% in November, compared to the 4% upper limit of the band. Analysts note that the increase in inflation is mostly due to the ruble's depreciation and that demand is likely to remain weak in coming months. **The Russian ruble weakened -1.3% to the dollar following the decision.**

Rates on Hold as Inflation Pops Above Target



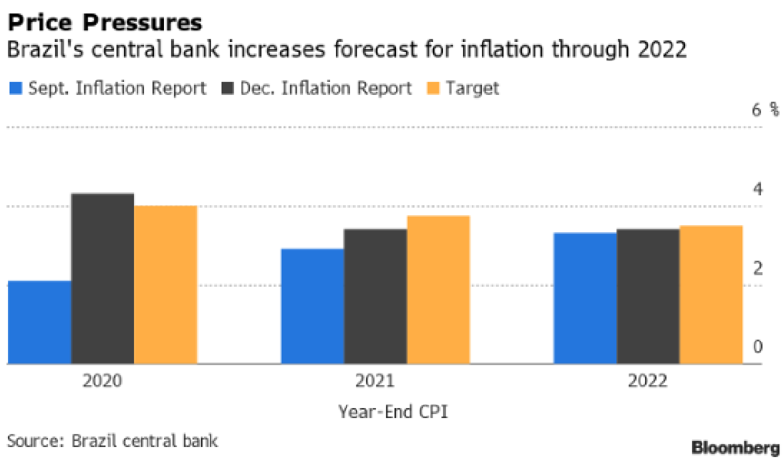
Source: Federal Statistics Service, Bank of Russia, Bloomberg Economics

Mexico

Mexico's central bank kept its policy rate unchanged at 4.25% on Thursday, in a 3-2 split decision. The decision was in line with market expectations, and the two dissenting votes were for cutting the policy rate by 25 bps to 4.0%. In the statement, the MPC restated the economy is facing challenges given the coronavirus-related risks to inflation, economic activities, and financial markets, and this pause in rate-cutting would provide "the necessary room to confirm that the trajectory of inflation converges to the target". Also, the MPC stated that future monetary policy decisions would depend on the new inflation data. Analysts commented that this was just a "tactical pause" and expected Banxico to resume the easing cycle soon. Mexican assets saw gains yesterday as the domestic equities rose 1.2% and the peso slightly appreciated against the dollar.

Brazil

The central bank revised up its inflation forecasts for the next two years, according to the quarterly inflation report released yesterday. Policy makers expect inflation to rise by 3.4% for both 2021 and 2022, with the inflation targeting 3.75% and 3.5%, respectively. Also, economists expect GDP to expand by 3.8% in 2021 (vs. 3.9% forecast in September) and forecast the Selic rate to be 4.5% by the end of 2022. Brazilian assets saw gains on Thursday, with the equity index rising 0.5% and the real appreciating 0.4% against the dollar.



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Global Financial Indicators

Last updated: 12/18/20 8:09 AM	Level		Change				
	Last 12m	Latest	1 Day	7 Days	30 Days	12 M	YTD
Equities			%				%
United States		3722	0.6	2	4	17	15
Europe		3566	0.2	2	2	-5	-5
Japan		26763	-0.2	0	4	12	13
China		3395	-0.3	1	1	13	11
Asia Ex Japan		88	0.6	0	4	21	20
Emerging Markets		51	0.7	0	5	15	14
Interest Rates			basis points				
US 10y Yield		0.93	-0.7	3	6	-99	-99
Germany 10y Yield		-0.57	0.2	7	-1	-32	-38
Japan 10y Yield		0.01	-0.1	0	-1	2	2
UK 10y Yield		0.25	-4.1	7	-9	-53	-58
Credit Spreads			basis points				
US Investment Grade		101	0.1	-5	-10	-3	3
US High Yield		396	0.0	-8	-51	-3	3
Europe IG		48	0.6	-3	-2	3	4
Europe HY		247	6.2	-20	-34	36	39
EMBIG Sovereign Spread		353	-4.0	-11	-26	60	64
Exchange Rates			%				
USD/Majors		89.90	0.1	-1	-3	-8	-7
EUR/USD		1.23	-0.1	1	3	10	9
USD/JPY		103.3	-0.2	1	0	6	5
EM/USD		57.9	0.0	1	3	-5	-6
Commodities			%				
Brent Crude Oil ($/barrel)		51	-0.3	3	16	-22	-22
Industrials Metals (index)		138	0.7	3	9	21	21
Agriculture (index)		45	0.3	3	1	9	8
Implied Volatility			%				
VIX Index (%, change in pp)		21.9	0.0	-1.4	-1.9	9.3	8.1
US 10y Swaption Volatility		57.0	0.2	-4.8	2.0	-3.2	-5.0
Global FX Volatility		8.1	0.0	-0.1	0.4	2.4	2.2
EA Sovereign Spreads			10-Year spread vs. Germany (bps)				
Greece		122	6.2	-2	0	-33	-44
Italy		113	1.8	-7	-8	-46	-47
Portugal		61	2.7	1	0	-3	-2
Spain		61	1.5	-2	-2	-7	-4

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: 12/18/2020 8:12 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		6.54	-0.1	0.1	0	7	6		3.4	0.0	0	-2	15	24
Indonesia		14110	0.0	-0.2	0	-1	-2		6.0	-0.2	-13	-26	-138	-112
India		74	0.0	0.1	1	-4	-3		6.0	-0.5	1	-4	-106	-91
Philippines		48	-0.1	0.0	0	5	5		3.6	-1.3	0	2	-62	-66
Thailand		30	0.1	0.7	2	1	0		1.4	-2.3	-9	-10	-31	-25
Malaysia		4.04	-0.1	0.2	1	2	1		2.6	-2.2	-7	4	-86	-79
Argentina		83	-0.1	-0.7	-3	-28	-28		56.7	34.2	193	393	-2091	-591
Brazil		5.11	-0.8	-0.9	5	-20	-21		5.8	0.9	-9	-54	-52	-43
Chile		724	-0.4	1.2	5	4	4		2.8	-4.0	-14	-2	-45	-54
Colombia		3412	0.2	0.8	7	-2	-4		5.2	-2.3	-2	-4	-74	-78
Mexico		19.85	-0.2	1.4	2	-4	-5		5.7	-2.9	-12	-40	-124	-128
Peru		3.6	0.0	0.2	0	-7	-8		3.6	-5.2	-21	-48	-91	-97
Uruguay		42	0.2	0.3	1	-11	-12		7.4	1.5	0	-10	-353	-350
Hungary		291	-0.6	0.4	4	2	1		1.5	-0.9	-9	-11	46	33
Poland		3.64	-0.7	0.8	3	5	4		0.6	-2.6	-7	4	-116	-124
Romania		4.0	-0.1	1.2	3	8	7		2.8	-5.0	-10	-14	-132	-124
Russia		73.5	-0.9	-0.8	3	-15	-16		5.6	-1.0	0	5	-59	-53
South Africa		14.6	0.5	3.9	6	-2	-4		9.6	-8.3	-22	-25	-3	6
Turkey		7.66	0.5	2.4	1	-23	-22		13.2	-18.1	-29	79	120	148
US (DXY; 5y UST)		90	0.1	-1.1	-3	-8	-7		0.37	-0.8	0	-3	-136	-132

	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		5000	-0.3	2	2	24	22		206	-1	0	-5	29	30
Indonesia		6104	-0.1	3	10	-3	-3		186	-2	-7	-5	27	30
India		46961	0.2	2	6	13	14		154	1	1	-19	29	29
Philippines		7273	-0.3	0	3	-6	-7		107	-2	-9	-5	41	41
Malaysia		1652	-1.3	-2	3	3	4		111	-2	-6	-9	-5	-1
Argentina		53116	-0.2	-1	4	41	27		1380	5	-13	23	-528	-389
Brazil		118401	0.5	3	12	4	2		251	-1	-10	-18	42	36
Chile		4223	2.1	3	3	-11	-10		147	2	-5	-3	9	14
Colombia		1444	1.6	5	17	-12	-13		206	-1	-9	-7	45	43
Mexico		44326	1.2	2	5	-2	2		384	0	-20	-50	92	92
Peru		20812	0.6	0	12	3	1		141	2	-14	-2	35	34
Hungary		42035	-0.1	2	10	-8	-9		97	1	-3	-6	10	11
Poland		55810	-0.7	1	7	-2	-3		3	0	-2	-7	-13	-15
Romania		9666	0.2	2	8	-2	-3		205	-4	-8	-2	24	31
Russia		3264	-0.6	0	6	8	7		163	3	-8	-15	34	32
South Africa		59868	-1.1	1	4	4	5		379	1	-5	-43	53	59
Turkey		1406	0.5	3	9	27	23		459	-2	-38	-42	55	58
Ukraine		508	0.0	0	1	0	0		485	4	-7	-89	61	65
EM total		51	0.0	0	5	15	14		353	-4	-11	-26	60	64

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

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