Global Markets Monitor

Monetary and Capital Markets Department
Global Markets Analysis Division

Wednesday, December 19, 2018

- **Italian government and EC reportedly reach agreement on budget deficit (link)**
- **Softbank disappoints in Japan's largest-ever IPO (link)**
- **Mexican government bonds rally despite global risk-off sentiment (link)**
- **Bank of Thailand raises its policy rate by 25 bps to 1.75%, as expected (link)**
- **Hungarian central bank keeps interest rates unchanged, as expected (link)**

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Global markets broadly stable ahead of today's FOMC meeting

Sentiment remains cautious following yesterday's 7% decline in oil prices, which spilled over to broader credit markets. US equities were flat following yesterday's volatile session. During the overnight session, Asian equities were mixed and European shares lackluster—outside of Italy, where equities outperformed regional peers and 10-year spreads to German bunds narrowed to 259 bps on reports of a technical budget agreement with the European Commission. US Treasury yields were lower and the dollar modestly weaker ahead of today's FOMC meeting. Market expectations are for a 25 bps interest rate hike, a more cautious and data dependent stance, and a modestly lower dotplot. Interest rate futures markets are pricing in a 50% chance of one rate increase for 2019, versus three rate hikes in the current dotplot from the September FOMC meeting. In EMs, markets traded with a muted tone. The central bank of Thailand hiked rates 25 bps and Hungary left policy rates unchanged, both as expected, with little market reaction.

Key Global Financial Indicators

Last updated: 12/19/18 7:58 AM	Level		Change from Market Close				YTD
	Last 12m	Latest	1 Day	7 Days	30 Days	12 M	
Equities					%		%
S&P 500		2546	0.0	-3	-5	-5	-5
Eurostoxx 50		3062	0.7	-1	-3	-15	-13
Nikkei 225		20988	-0.6	-3	-4	-8	-8
MSCI EM		39	0.4	-2	-3	-14	-17
Yields and Spreads					bps		
US 10y Yield		2.82	-4.0	-9	-25	35	41
Germany 10y Yield		0.24	-0.3	-4	-13	-14	-19
EMBIG Sovereign Spread		397	0	3	12	118	112
FX / Commodities / Volatility					%		
EM FX vs. USD, (+) = appreciation		62.1	0.0	0	-1	-10	-11
Dollar index, (+) = $ appreciation		96.9	-0.3	0	1	5	5
Brent Crude Oil ($/barrel)		56.5	0.4	-6	-15	-11	-16
VIX Index (%, change in pp)		25.1	-0.5	4	5	15	14

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

United States

Risk sentiment remained fragile on Tuesday, as investors continue to scale back expectations for Fed interest rate hikes. Treasuries continued to rally strongly and the curve steepened as the market prepared for the outcome of today's FOMC meeting. Yields declined 5 bps at the 2-year tenor and 4 bps at the 10-year tenor, with the latter just shy of its lowest level since May (2.82%). **Market-implied expectations for Fed rate hikes in 2019 and 2020 declined substantially,** even as expectations for a rate hike today remained intact. Eurodollar markets saw a decline of 6 bps in the December 2019 contract and 11 bps in the December 2020 contract (with 12 bps of Fed rate cuts priced in for 2020). The fed funds futures market now prices less than a 50% chance of a single 25 bps hike for all of next year.

Mid Yield To Maturity
EDZ9 Comdty (90DAY EURO$ FUTR Dec19) 2.7750
FFZ9 Comdty (FED FUND 30DAY Dec19) 2.5150
EDZ0 Comdty (90DAY EURO$ FUTR Dec20) 2.6550

EDZ9 Comdty (90DAY EURO$ FUTR Dec19) Daily 18JUN2018-18DEC2018   Copyright© 2018 Bloomberg Finance L.P.   18-Dec-2018 19:47:35

US equities ended the day flat after a volatile session. The S&P 500 started with gains following stronger than expected housing data but swung nearly 2% from peak to trough before closing unchanged, around the low for 2018, bringing year to date performance to -4.75%. A nearly 8% intra-day decline in the price of oil, spurred by strong supply in the US and Russia, added gloom to the growth outlook and weighed heavily on energy shares, which lost -2.3%. **The VIX rose by one point to 25.6, its highest close since February's volatility tantrum**. High-yield corporate bonds also came under pressure, with spreads to treasuries widening 17 bps to 464 bps – led by weak performance in the energy sector (+33 bps). **HY bond spreads have now widened 148 bps so far this quarter**, and are at their widest level since November 2016.

The **risk of a government shutdown starting midnight this Friday continues** as lawmakers and the white house appear unable to agree on a stopgap funding measure.

Europe

European bourses are up: EuroStoxx 600 (+0.2%), DAX (+0.4%), and CAC 40 (+0.3%). Stocks in Italy (+1.5%) are strongly outperforming peers, with Italian bank stocks advancing 2.7% vs. 0.9% for European banks.

Core eurozone sovereign yields are little changed while Italian yields dropped notably following news of a possible agreement between the government and the EC (see below). Ten-year bonds are at 2.84% (-

12 bps) and 2-year yields at 0.47% (-8 bps); the 10-year spread between Italian and German bonds has thus narrowed to 259 bps.

Italy-Germany Sovereign Spreads
(in bps)

Source: Bloomberg
CFRTR1U5 Curncy (FRANCE CDS USD SR 5Y D14) FI: Ita-Germ Spreads Daily 29DEC2017   Copyright© 2018 Bloomberg Finance L.P.   19-Dec-2018 10:44:24

The Italian government and the EC have reportedly reached an agreement on the country's budget, according to various media outlets. Details are scant at the moment and there has not been an official statement on the deal. The press reports, however, that a 2019 deficit of 2.04% would have been agreed upon, along with a pledge by the Italian government to seek €2 bn in privatization receipts. A formal announcement is expected later today.

With only 100 days to go before Brexit, **UK equities gained today** – FTSE 100 (+0.8%) and FTSE 250 (+0.3%) – **while 10-year gilt yields stayed at 1.26%.** For the year, the FTSE 100 is poised to close over 10% lower. Sterling is at $1.27 (+0.1%) – close to its weakest level since mid-2017.

Cost of Uncertainty
U.K. stocks are poised for the deepest annual drop since the 2008 crisis

Source: Bloomberg
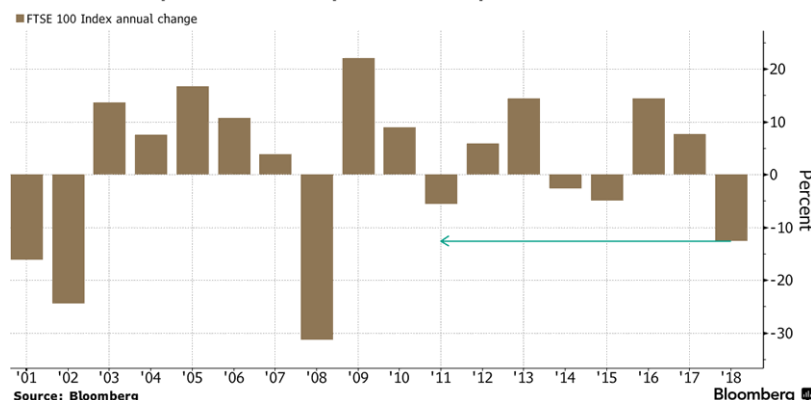
British Pound vs US Dollar

GBP Curncy (British Pound Spot) FX: GBP post Brexit v2 Daily 13JAN2016-19DEC201   Copyright© 2018 Bloomberg Finance L.P.   19-Dec-2018 10:32:18
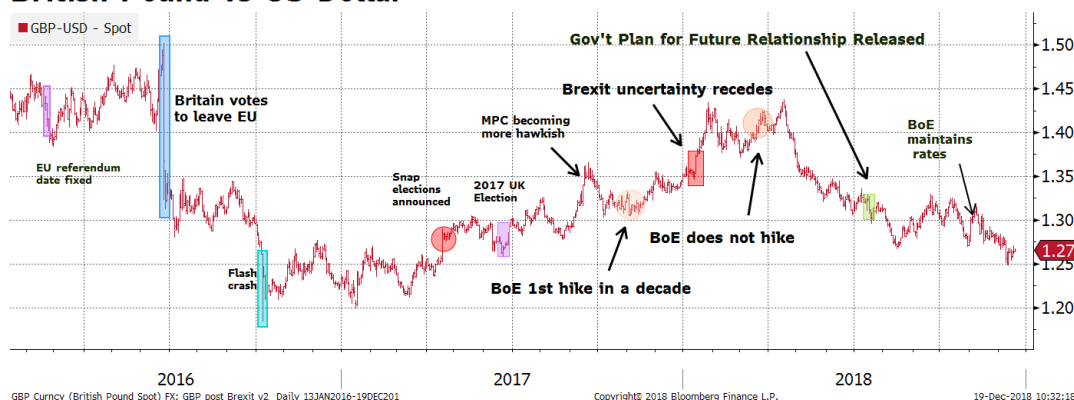
Other Mature Markets   back to top

Japan

Equities declined (Nikkei -0.6%, Topix -0.4%) and Softbank's mobile unit IPO disappointed. The listing of $23.5 bn in shares of Softbank Corp was Japan's largest-ever IPO. Shares closed 15% lower than the IPO price. On a sectoral basis, energy stocks declined the most on falling oil prices. **The yen appreciated 0.1% against the dollar. 10-year JGB yields rose 1 bp to 0.022%.**

Stocks Drop
Nikkei 225 dips below 21,000 for the first time since March

Source: Bloomberg

Emerging Markets   back to top

Key Emerging Market Financial Indicators

Last updated: 12/19/18 7:59 AM	Level Last 12m	index	1 Day	7 Days	30 Days	12 M	YTD
Major EM Benchmarks				%			%
MSCI EM Equities		39.14	0.4	-2	-3	-14	-17
MSCI Frontier Equities		26.93	0.8	-2	-1	-18	-19
EMBIG Sovereign Spread (in bps)		397	0	3	12	118	112
EM FX vs. USD		62.15	0.0	0	-1	-10	-11
Major EM FX vs. USD			%, (+) = EM currency appreciation				
China Renminbi		6.90	-0.1	0	1	-4	-6
Indonesian Rupiah		14439	0.4	1	1	-6	-6
Indian Rupee		70.40	0.1	2	2	-9	-9
Argentine Peso		38.27	-0.1	-1	-6	-54	-51
Brazil Real		3.90	0.2	-1	-4	-16	-15
Mexican Peso		20.09	-0.1	0	1	-4	-2
Russian Ruble		67.53	-0.2	-2	-3	-13	-15
South African Rand		14.27	0.6	-1	-2	-11	-13
Turkish Lira		5.34	0.2	0	0	-28	-29
EM FX volatility		9.67	0.0	-0.5	-0.5	2.1	1.8

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

In **Asia,** equities gained (+0.6%) as declines in China were offset by gains in most of the other regional markets**.** Chinese equities sold off in both Shanghai (-1.4%) and Shenzhen (-1.1%) on little apparent news flow. The region's strongest performing markets were in South East Asia: Philippines (+2.1%), Indonesia (+1.5%), and Malaysia (+1.2%). In FX markets, the Korean won outperformed (+0.6%) and the Indian rupee

(+0.2%) and the Indonesian rupiah (+0.5%) continued to appreciate against the dollar on lower oil prices. Sovereign bond yields declined across the region, with notable drops in India (-12 bps) and Indonesia (-11 bps). The Bank of Thailand raised its policy rate by 25 bps to 1.75% in its first hike since 2011. In **EMEA**, bourses mostly advanced, led by strong gains in the Czech Republic (+2.0%). Currencies strengthened somewhat versus the US dollar. Oman's credit rating was downgraded by Fitch, which will result in exclusion from IG-only indices. **Latin American** equity markets moved higher in line with the US, with Mexican stocks outperforming regional peers**.** Argentina's Q3 GDP estimate met consensus expectations of -3.5% yoy and did not elicit much market reaction. Minutes from the latest BCB meeting showed that the central bank remains worried about signs of inflation, despite recent data prints coming in below target.

Mexico

Mexican government bond yields have continued to edge lower in response to the new budget, despite volatility in global markets. Contacts reported strong buying interest from international investors, marking a reversal in the recent pullback that accompanied the government's decision on the airport project. Longer-dated bonds have been especially popular among investors, as they benefit the most from the repricing in duration risk. The consensus is that rating downgrade risk is now much lower. Most analysts predict that Thursday's expected 25 bps Banxico rate hike will be the last for the current cycle.

MBono 2036 Yield
Source: Bloomberg
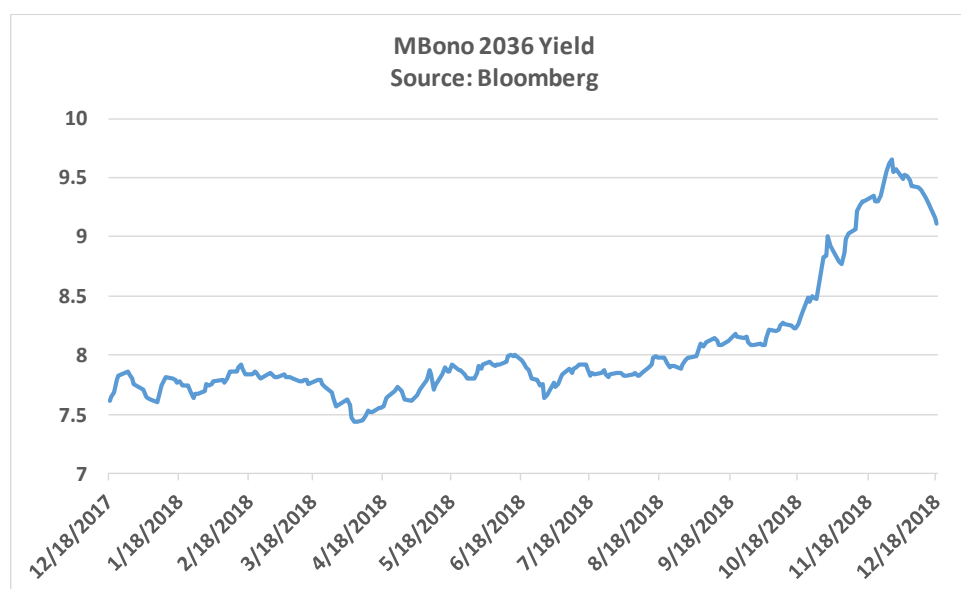
Thailand

The Bank of Thailand (BoT) raised its policy rate by 25 bps to 1.75%, marking its first hike since 2011. The vote split was 5-2, versus 3-4 at the November meeting, with two members of the monetary policy committee voting to leave the policy rate unchanged. The BoT also lowered its GDP growth forecast to 4.2% for 2018 from 4.4% and its 2019 forecast to 4.0% from 4.2%. The BoT maintained its 2018 headline CPI inflation forecast of 1.1% but trimmed its 2019 forecast to 1.0% from 1.1%. Previous BoT policy statements had indicated growing concerns over financial stability risks associated with low rates. Analysts expect the BoT to pause after this hike given slowing growth and inflation potentially falling below the BoT's 1-4% target band. **The asset price reaction to the expected rate hike was muted**: stocks gained 1.1%, while the baht and sovereign bond yields were little changed.

The Hungarian central bank kept interest rates unchanged, as expected. Policy rates were left at 0.9% for the required reserves and 0.15% for the overnight deposit rate. The central bank left its projection of

inflation for 2018 unchanged at 2.8% while it lowered the 2019 estimate to 2.9% from 3.1% previously. The growth forecast for 2018 was upgraded to 4.7% (from 4.4%). Equities and the forint are both 0.2% higher today.

Hungary sticks to dovish monetary policy

■Hungary annual inflation rate ■3-month interbank rate

Source: Bloomberg   Bloomberg
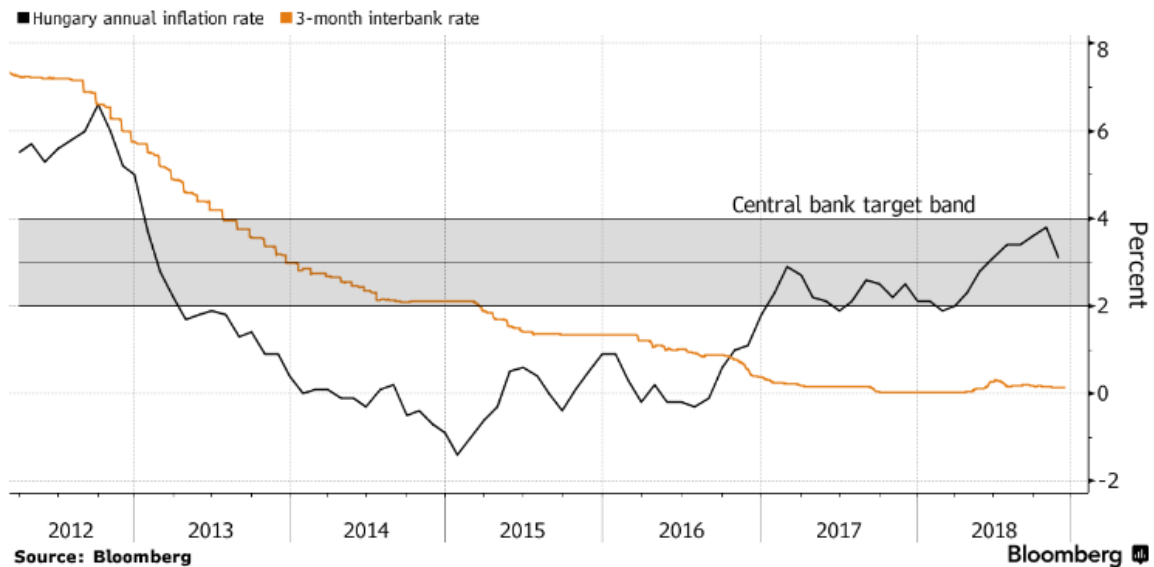
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Global Financial Indicators

Last updated: 12/19/18 8:00 AM	Level		Change				
	Last 12m	Latest	1 Day	7 Days	30 Days	12 M	YTD
Equities				%			%
United States		2546	0.0	-3	-5	-5	-5
Europe		3062	0.7	-1	-3	-15	-13
Japan		20988	-0.6	-3	-4	-8	-8
China		2550	-1.1	-2	-6	-23	-23
Asia Ex Japan		64	0.5	-2	-2	-14	-16
Emerging Markets		39	0.4	-2	-3	-14	-17
Interest Rates				basis points			
US 10y Yield		2.82	-4.0	-9	-25	35	41
Germany 10y Yield		0.24	-0.3	-4	-13	-14	-19
Japan 10y Yield		0.04	0.9	-2	-6	-1	-1
UK 10y Yield		1.27	-0.7	-1	-11	7	8
Credit Spreads				basis points			
US Investment Grade		137	1.8	-1	21	44	46
US High Yield		464	13.2	23	51	86	89
Europe IG		81	-1.2	0	1	34	36
Europe HY		337	-5.7	9	10	102	104
EMBIG Sovereign Spread		397	0.0	3	12	118	112
Exchange Rates				%			
Dollar Index (DXY)		96.85	-0.3	0	1	4	5
USDEUR		1.14	0.3	0	0	-4	-5
USDJPY		112.4	0.1	1	0	0	0
EM FX vs. USD		62.1	0.0	0	-1	-10	-11
Commodities				%			
Brent Crude Oil ($/barrel)		56	0.4	-6	-15	-11	-16
Industrials Metals (index)		112	0.3	-2	-3	-14	-19
Agriculture (index)		43	-0.2	-1	1	-9	-10
Implied Volatility				%			
VIX Index (%, change in pp)		25.1	-0.5	3.6	5.0	15.1	14.1
10y Treasury Volatility Index		4.1	0.1	-0.2	-0.3	0.7	0.6
Global FX Volatility		8.4	0.0	-0.3	-0.3	1.3	1.0
EA Sovereign Spreads				10-Year spread vs. Germany (bps)			
Greece		405	-9.0	6	-15	32	36
Italy		252	-17.3	-20	-70	99	93
Portugal		139	-0.3	-5	-22	-6	-13
Spain		112	-1.1	-3	-15	2	-2

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

Emerging Market Financial Indicators

Last updated: 12/19/2018 8:01 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	-0.1	-0.3	1	-4	-6		3.3	0.8	6	-8	-71	-70
Indonesia		14439	0.4	1.1	1	-6	-6		8.2	-7.2	-13	-1	148	161
India		70	0.1	2.3	2	-9	-9		7.5	-4.0	-13	-35	16	2
Philippines		53	0.0	-0.7	-1	-5	-6		6.3	-0.4	5	-29	152	149
Thailand		33	0.0	0.1	1	0	0		2.7	-2.3	0	-16	38	42
Malaysia		4.18	-0.1	0.1	0	-2	-3		4.1	-1.0	-1	-6	19	21
Argentina		38	-0.1	-1.2	-6	-54	-51		23.3	-2.6	-8	-67	724	724
Brazil		3.90	0.2	-1.2	-4	-16	-15		8.4	5.9	-22	-14	-77	-62
Chile		688	0.1	-1.5	-3	-10	-11		4.6	-2.5	-3	-19	-31	-22
Colombia		3206	-0.8	-0.6	-1	-7	-7		6.6	0.5	-5	-15	45	35
Mexico		20.09	-0.1	-0.1	1	-4	-2		8.8	-10.7	-30	-22	130	115
Peru		3.3	-0.2	0.4	1	-2	-3		5.8	-0.4	-6	5	45	61
Uruguay		32	0.1	0.0	1	-11	-11		10.9	-0.6	-10	8		231
Hungary		283	0.1	0.3	-1	-7	-9		2.4	1.8	8	-26	114	115
Poland		3.76	0.3	0.5	1	-6	-7		2.3	-2.5	-10	-31	-34	-36
Romania		4.1	-0.1	0.0	0	-5	-5		4.0	0.0	-4	-34	17	21
Russia		67.5	-0.2	-1.6	-3	-13	-15		8.5	2.6	9	10	118	121
South Africa		14.3	0.6	-1.1	-2	-11	-13		9.8	-11.3	-3	13	42	50
Turkey		5.34	0.2	0.2	0	-28	-29		18.2	-10.9	2	132	577	622
US (DXY; 5y UST)		97	-0.3	-0.2	1	4	5		2.65	0.5	-12	-22	43	44

	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		2550	-1.1	-2	-6	-23	-23		191	-3	1	4	49	39
Indonesia		6176	1.5	1	3	0	-3		220	-1	-9	-5	57	54
India		36484	0.4	2	2	8	7		189	-2	3	15	79	79
Philippines		7580	2.1	1	4	-9	-11		113	2	-2	-2	25	18
Malaysia		1656	1	0	-3	-5	-8		154	-4	5	12	52	44
Argentina		29777	-0.4	-4	-4	7	-1		787	-1	46	114	436	437
Brazil		87250	0.2	0	-1	20	14		262	0	2	0	34	28
Chile		5113	0.2	0	-1	-8	-8		156	-4	-3	5	40	37
Colombia		1336	0.0	-3	-6	-9	-12		207	-1	11	-6	39	33
Mexico		40918	1.4	-1	-3	-15	-17		330	-1	7	-9	92	85
Peru		19157	0	0	-1	0	-4		157	-1	-4	-10	22	20
Hungary		39536	0.2	-1	1	2	0		140	-3	-3	-3	58	52
Poland		58990	0.5	2	6	-7	-7		77	-4	8	8	39	30
Romania		7403	-12.1	-14	-14	-5	-5		210	1	-11	6	93	96
Russia		2344	-0.3	-1	-1	11	11		244	-1	2	7	68	66
South Africa		51511	0.6	1	-2	-11	-13		356	-3	-1	3	106	102
Turkey		91631	0.6	2	-3	-17	-21		445	-9	-13	-1	155	156
Ukraine		566	0.1	-1	-2	83	80		742	3	1	97	285	287
EM total		24	0.0	-1	-2	-11	-11		397	0	3	12	118	112

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

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