GLOBAL MARKETS ANALYSIS
Monetary and Capital Markets

Global Markets Monitor

WEDNESDAY, DECEMBER 2, 2020

- **Treasury yields rise on renewed hope for stimulus package** (link)
- **European credit spreads continue to tighten on positive investor sentiment** (link)
- **No plans for immediate removal of China tariffs under Biden administration** (link)
- **US banks' margin compression accelerates despite record low funding costs** (link)
- **Russian money markets show signs of stress despite abundant ruble liquidity** (link)
- **Prospects for stronger fiscal stance support Brazilian Real outperformance** (link)

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

Risk rally slows as investors eye political developments

Following yesterday's rally, risk assets are trading on the heavy side today. Positive news regarding the approval of a COVID-19 vaccine in the UK—the first western country to do so—and possible renewed traction on the fiscal stimulus front in the US seem to be outweighed by other developments, including reported statements by an EU official that raised doubts about the successful conclusion of a Brexit deal, as well as comments by the US President-Elect that seemed to tone down market expectations of any imminent reversal of the Phase-1 US tariffs on China. European equities are slightly down this morning, while EM stocks are mixed and US equity futures are pointing to a weak start. The GBP is about 1% weaker against the greenback, while the EUR seems to be holding on to yesterday's impressive 1.2% gain (+7.6% YTD). And while developed-market sovereign paper seems to be holding steady today, this follows a trading session during which 10-Year Treasury yields rose by 8 bps and the 2Y-10Y spread steepened by 7 bps. It is notable that 10-Year US breakeven rate—a measure of market inflation expectations—increased by about 7 bps this week to 1.83%, compared to 0.51% at its trough in March. On the commodities front, gold is up slightly today (+2% WTD) while crude oil prices are holding steady as investors await tomorrow's conclusion of the OPEC+ meeting.

Key Global Financial Indicators

Last updated: 12/2/20 8:42 AM	Level: Last 12m	Level: Latest	Change from Market Close: 1 Day	7 Days	30 Days	12 M	YTD
Equities					%		%
S&P 500		3662	1.1	2	11	18	13
Eurostoxx 50		3503	-0.6	0	16	-3	-6
Nikkei 225		26801	0.1	2	15	14	13
MSCI EM		50	2.0	1	10	18	11
Yields and Spreads					bps		
US 10y Yield		0.93	0.7	5	9	-89	-98
Germany 10y Yield		-0.52	1.0	5	12	-24	-33
FX / Commodities / Volatility					%		
EM FX vs. USD, (+) = appreciation		56.7	-0.1	1	5	-6	-8
Dollar index, (+) = $ appreciation		91.3	0.0	-1	-3	-7	-5
Brent Crude Oil ($/barrel)		47.3	-0.3	-3	21	-22	-28
VIX Index (%, change in pp)		21.1	0.3	-1	-16	6	7

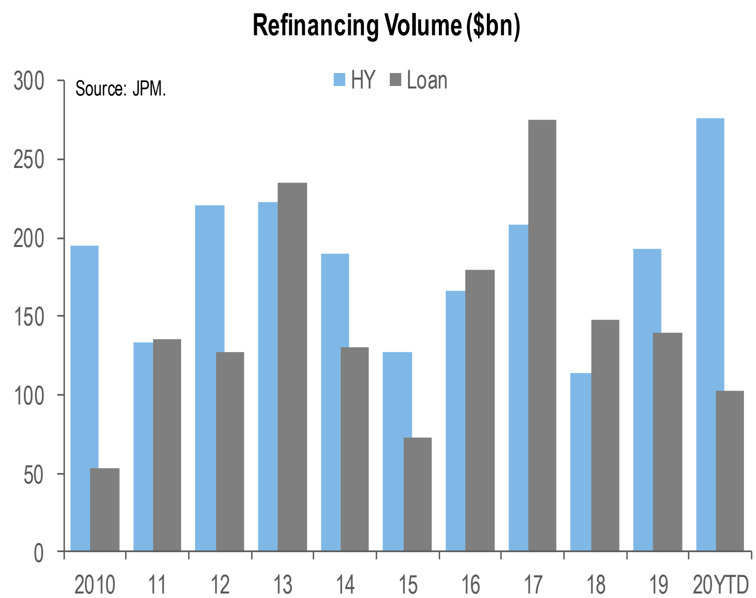
Colors denote tightening/easing financial conditions for observations greater than ±1.5 standard deviations. Data source: Bloomberg.

United States

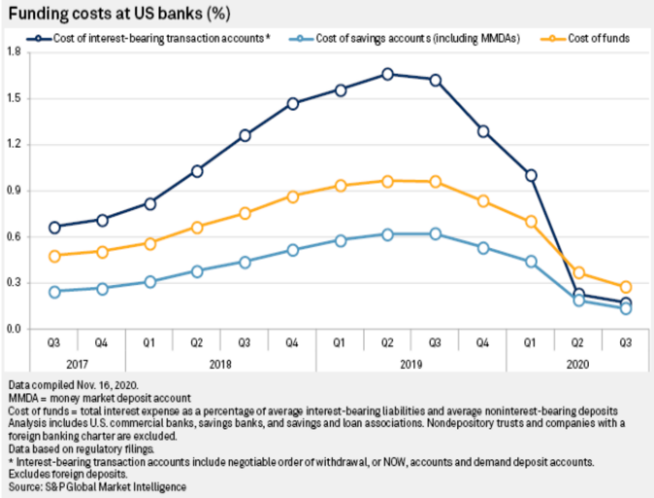
back to top

Global stocks closed markedly higher amid a sharp spike in sovereign yields, as investors continued to seek out more risk, while the dollar extended its slide towards a two-year low. Growth stocks, especially the large cap tech, were leading the way today, followed by financials which benefited from the rise in rates. The continuing sectoral rotation is seen a healthy sign that keeps the bull market alive. Markets pared back some gains in the final hour as news that 3 separate US stimulus packages emerged – one bipartisan offer of $908 bn, one from House Speaker Pelosi and one from Senate Majority Leader McConnell, neither of which offered any detail – highlighting the lingering stalemate in the debate. The S&P 500 and NASDAQ rose 1.2%, both closing at record highs. Treasuries sold off, particularly the long-end bonds, with the curve steepening by 2 to 9 bps across tenors. The 10-year breakeven rate (a measure of market-expected inflation) climbed to 1.8%, its highest level since May 2019. Yesterday's price action came despite a weaker-than-expected ISM report (-1.8 pts to 57.5 vs 58 expected), indicating that investors seem to be looking through the potential short-term pains from the second wave of COVID-19 and positioning for a return to normal scenario next year following a national rollout of the vaccine. The US dollar took another decisive leg lower, with the DXY down 0.7% on the day – lowest since April 2018.

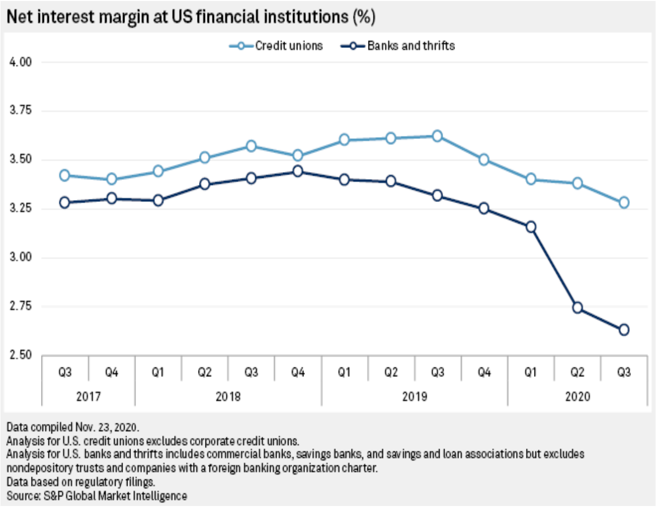
Speculative debt refinancing volume reached a record this year as issuers capitalized on the collapse in yields. After reaching a record $37 bn in June, refinancing volume totaled an unprecedented $44.6 bn in August and $40.9 bn in September. With yields down an additional 100 bps during Q4, refinancing has continued to dominate primary market activities, bringing the YTD total to $275.5 bn, which is 20% above the previous record high in 2013.



Awash in liquidity, funding costs for US banks plummeted close to the zero-lower bound. Total deposits across the industry increased $152 bn to $15.6 tn in Q3, with growth in transaction and savings deposits more than offsetting declines in time deposits. Commercial banks added roughly another $275 bn in deposits in the first six weeks of Q4, according to weekly Federal Reserve data, with ongoing asset purchase by the central bank. In response, deposit costs plummeted to 14 bps in Q3, lowest level in more than 5 years. The same is true for the overall cost of funds at 28 bps.



Margin compression accelerated for US banks. Net interest margin (NIM) for banks and thrifts fell further in Q3 to 2.6% (-70 bps /y), the lowest level since 2016. The banks' participation in the Paycheck Protection Program, which comprises around 5% of total loans and leases, has exacerbated this margin compression. In contrast, NIMs at credit unions remain relatively resilient, down 34 bps y/y to 3.28% in Q3. Credit unions specialize in consumer and mortgage lending, with a concentration in fixed-rate loans, making them better situated to moderate margin pressure in a declining rate environment.



Europe

back to top

Equity markets slumped with the main indices losing some ground. DAX (-0.3%), CAC 40 (-0.2%), EuroStoxx 600 (-0.2%), Italy's Titans 30 (-0.6%), and Spanish Ibex (unch). Bank stocks (-0.8%) slightly underperformed.

Sovereign yields traded mostly flat. German 10-year yields at -0.53% (-1 bps); French OATs are at -0.29% (-1 bps); Italian at 0.65% (-2 bps); and Spanish at 0.10% (-1 bps).

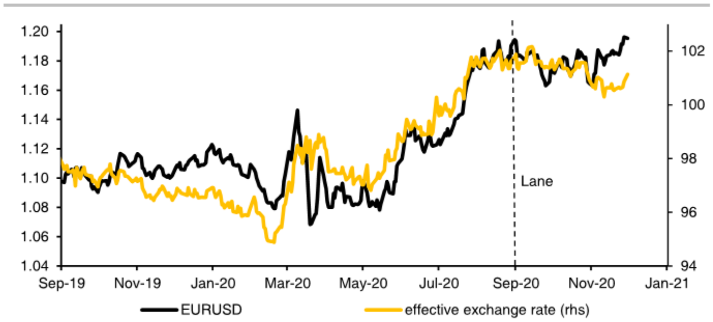
UK authorities have approved the new Pfizer-BioNTech Covid-19 vaccine. Reportedly, enough doses have been ordered to cover the first 20 million people (UK population is 67 million). The government is planning a prioritized delivery of the immunizations.

Here are the government's draft priority rankings:

- Residents in care homes and their carers
- All those 80 years of age and over, and frontline health and social-care workers
- All those 75 years of age and over
- All those 70 years of age and over. Clinically extremely vulnerable individuals
- All those 65 years of age and over
- All individuals aged 16 to 64 with underlying health conditions
- All those 60 years of age and over
- All those 55 years of age and over
- All those 50 years of age and over

The euro (-0.2%) pared some of yesterday's +1.2% move that breached the $1.20 barrier. The sizeable jump has stirred speculation in markets on whether the ECB will react to weaken the common currency. As the ECB's governing council prepares to meet next week, Governor Kazaks (Latvia) said that a €500 bn expansion of the ECB's PEPP would be "reasonable".

Lane unlikely to intervene as vigorously this time
Euro exchange rates

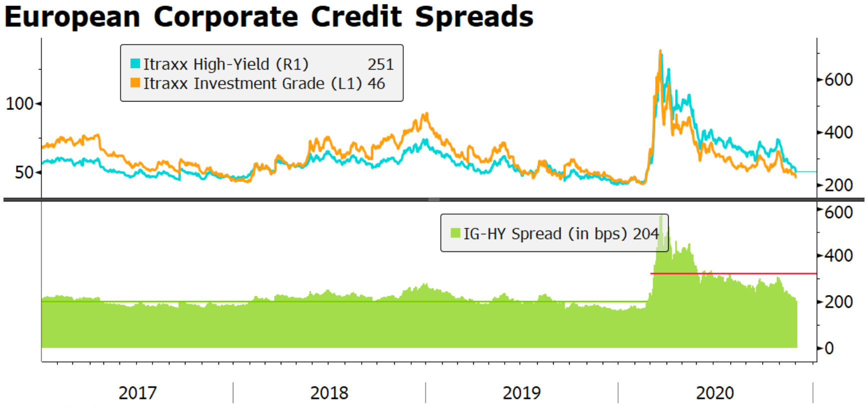


Source: Bloomberg, Commerzbank Research

The EU has approved €3.5 bn of further support for companies negatively affected by the pandemic. The new scheme will reportedly rely on subordinated loans and equity investments to aid these firms.

The rally in European credit markets has continued today on the back of an earlier-than-expected roll out of COVID vaccines. The high-yield corporate spread stood at 251 bps and investment grade at 46 bps. The differential between high-yield and investment grade, which had surged to about 600 bps as the pandemic broke out, has been closing and is approaching its medium-run average. Despite these market dynamics, **Moody's sees European default rates climbing over the next months.** The agency expects speculative-grade defaults to peak at 6% in Q1 2021 from around 4% currently.

European Corporate Credit Spreads



Source: Bloomberg
ITRXEXE Curncy (MARKIT ITRX EUR XOVER 12/25) Credit: Itraxx indices Daily 04JAN Copyright© 2020 Bloomberg Finance L.P. 02-Dec-2020 11:00:57

Other Mature Markets

back to top

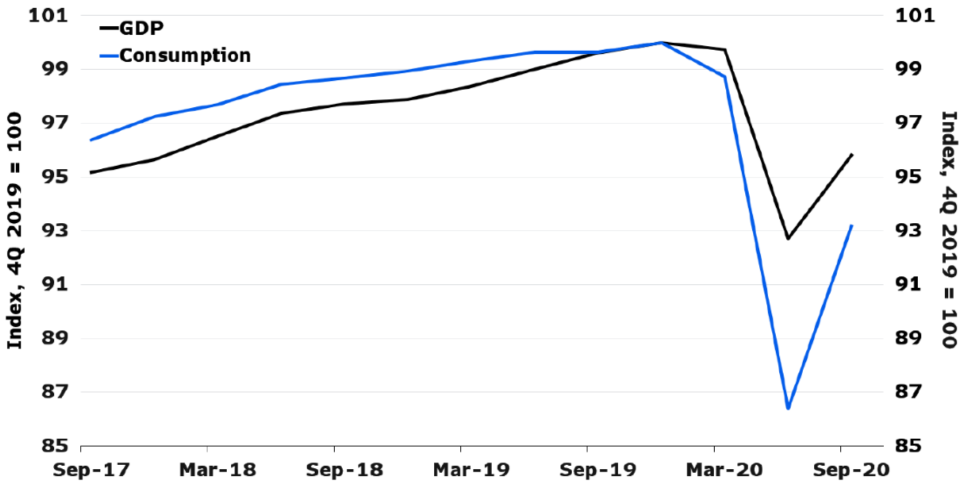
Japan

Japan's parliament passed a bill to provide free COVID vaccination. The central government will cover the cost, while local governments will be responsible for administering the vaccines. **Bank of Japan (BOJ) Deputy Governor Amamiya saw no need for additional monetary stimulus.** Amamiya, a key architect of the BOJ's massive stimulus under Governor Kuroda, said that the CPI looks resilient once special factors—raw foods, energy and government travel discounts—are accounted for. Adjusted CPI inflation would be in the range of 0.0%-0.5%, which is solid considering the degree of the economic contraction.

Australia

Real GDP expanded more than expected in 2020Q3. Real GDP increased by 3.3% q/q in Q3, beating expectations (2.5%) and reversing a 7.0% q/q decline in Q2. Growth was driven by household spending. Analysts noted that a further easing of restrictions in Q4 will support economic activity going forward. While seeing that the economy has turned a corner, Reserve Bank of Australia Governor Lowe cautioned against a bumpy recovery and mentioned that a period of protracted, high unemployment could undermine households' ability to repay debt.

Consumer-driven Economic Recovery Has Further to Run



Source: Bloomberg.

Emerging Markets

back to top

In **Asia,** stock markets did not have a clear direction. Share prices rose in Korea (+1.6%) and Indonesia (+1.6%), while equities declined in Malaysia (-0.2%) and Thailand (-0.2%). Asian currencies were also mixed. Korean won appreciated (+0.5%), while Singaporean dollar (-0.2%) and Indian rupee (-0.2%) depreciated. In Thailand, the court dismissed a petition seeking to disqualify the prime minister for allegedly breaking ethical rules, allowing him to stay in the office. The Thai baht was little changed.

In **EMEA,** equities were trading mixed with stocks up in Poland (+1.1%), South Africa (+0.8%) but down in Israel (-1.6%) and Saudi Arabia (-0.5%). EMEA currencies were little changed except for the South African rand which weakened by about 1% against the US dollar, giving up much of yesterday's gains.

In **Latin America**, regional equity indices rose by around 2% and currencies strengthened, tracking the risk on sentiment in global markets. The Brazilian real outperformed all EM currencies appreciating by 2.3%, after President Bolsonaro signaled to markets that congress won't extend some of the benefits that expire at year-end. The Chilean peso rose by 0.4% as copper prices continue to rally (14% over the past month and at a 7-year high).

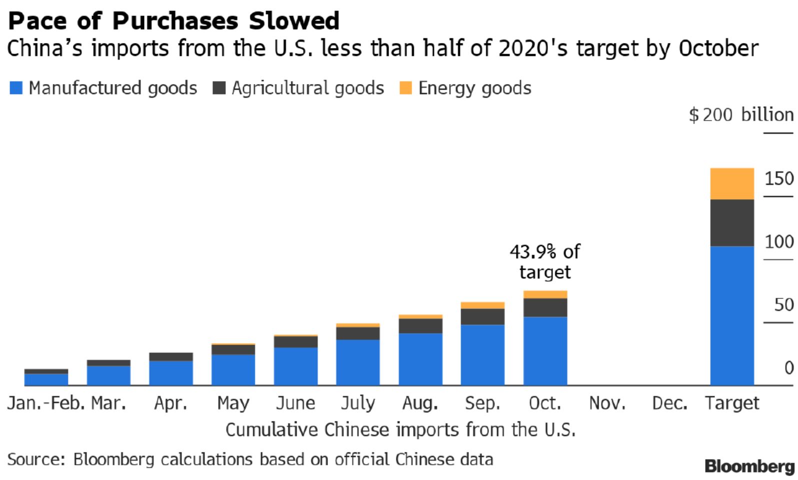
Key Emerging Market Financial Indicators

Last updated:	Level		Change				
12/2/20 8:45 AM	Last 12m	index	1 Day	7 Days	30 Days	12 M	YTD
Major EM Benchmarks					%		%
MSCI EM Equities		49.69	-0.1	1	10	18	11
MSCI Frontier Equities		27.58	1.4	0	6	-6	-9
EM FX vs. USD		56.69	-0.1	1	5	-6	-8
Major EM FX vs. USD				%, (+) = EM currency appreciation			
China Renminbi		6.56	0.1	0	2	7	6
Indonesian Rupiah		14125	0.0	0	4	0	-2
Indian Rupee		73.80	-0.2	0	1	-3	-3
Argentine Peso		81.47	0.0	-1	-3	-26	-27
Brazil Real		5.23	-0.1	2	10	-19	-23
Mexican Peso		20.10	-0.3	-1	6	-3	-6
Russian Ruble		75.58	0.3	0	7	-15	-18
South African Rand		15.37	-0.8	-2	6	-5	-9
Turkish Lira		7.85	-0.2	1	7	-27	-24
EM FX volatility		10.06	0.0	-0.1	-1.7	3.2	3.5

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

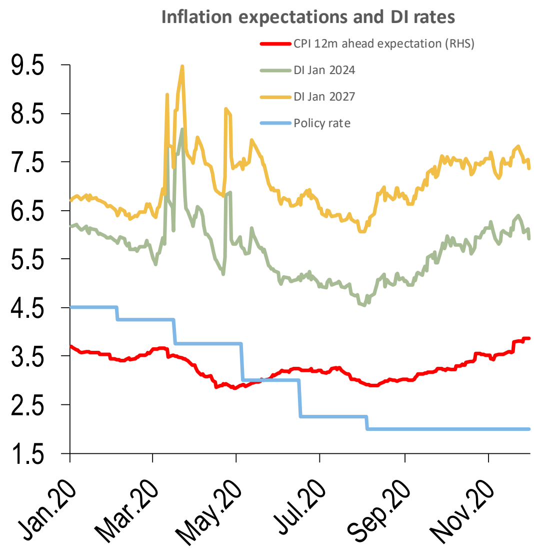
China

U.S. President-Elect Biden said that phase-one tariffs on China will not be quickly removed. Biden told the New York Times that he would leave the phase-one deal in place while conducting a full review of U.S. policy toward China in consultation with key allies. To date, China is still far behind its commitment on purchasing U.S. goods during 2020 (only at 44% of the target). Biden aims to evaluate China's current practices with respect to intellectual property and the provision of domestic subsidies. He also plans to develop bipartisan support for a government-led investment program in R&D and infrastructure that would help the U.S. better compete with China in the long-run.

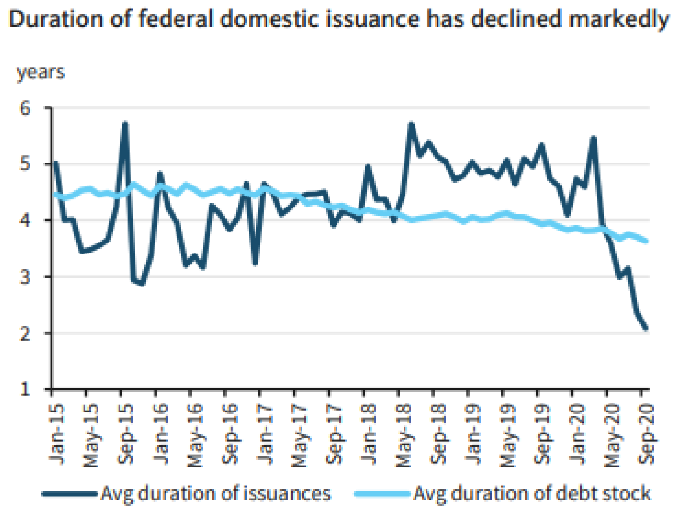


Brazil

The real continued its recent strong run—appreciating by another 2.3% on Tuesday—after President Bolsonaro signaled to markets that congress won't extend some of the benefits that expire at year-end. On the back of the global risk rally in November, the real has been the best performing EM currency appreciating by over 10%. The latest headlines increased market optimism that the government and the congress will find a compromise that reduces the fiscal uncertainty surrounding the 2021 budget. Since the beginning of last week, 2- to 5-year swap rates have shifted down by around 50bps. Risk premia in local rates however remain elevated, with long end rates at similar levels to early 2020 (pre-pandemic) despite 250bps of policy rate cuts in the interim. On Tuesday the treasury also issued 2023 inflation linked bonds that saw strong demand. The treasury has been planning to gradually lengthen the maturity of public debt, but investor demand remains centered around shorter maturities, floaters and inflation linkers given the high levels of uncertainty.



Source: Bloomberg

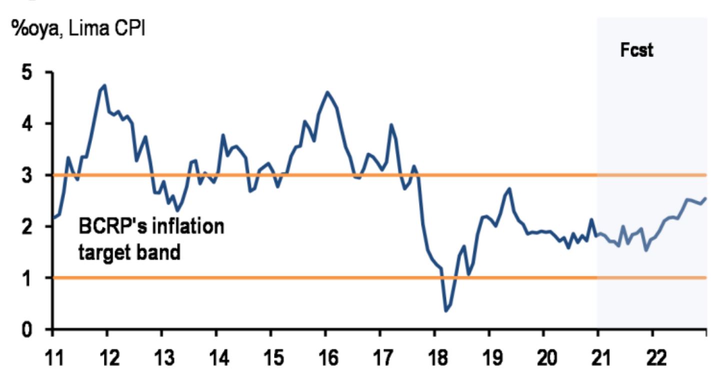


Source: Tesouro Nacional, Barclays Research

Peru

Lima CPI was higher-than-expected, increasing 0.5% m/m versus expectations of 0%. This upside surprise drove the over-year-ago CPI figure to 2.14% (1.8% y-o-y consensus), the highest print since mid-2019. There was no notable market reaction to the data release. Like other positive surprises seen in Latin America over the last few months, the main category driving the increase was Food and Beverage. JPM highlights that this category explained 67% of the CPI variation in November. The central bank held its policy rate at a record low 0.25% last month.

Figure 2: Peru CPI



Source: INEI, BCRP and J.P Morgan

Russia

Russian money markets continued to show signs of stress even as overall ruble liquidity remains loose. The spread of 3-month Mosprime fixing (equivalent of Libor) over the policy rate has reached 70 bps as compared to the usual range of 30-35 bps. The spread tends to increase during periods of tight ruble liquidity, anticipation of policy rate hikes or credit stress in the banking sector. Given that none of the above-mentioned factors are currently present, market participants have been puzzled by the move. Some contacts suggest that the stress in the money markets could be due to the combination of new regulatory liquidity ratio requirements and the large issuance by Russian state oil firm Rosneft in the local primary bond market. Last week, Rosneft issued a record of RUB 800 bn ($10.5 bn) of floating rate notes, the purchase of which may have triggered additional term-funding requirements among systemic banks as part of the liquidity ratio. **The fixing move has primarily affected the interest rate swap market where yields increased by 20 bps.**

Source: Bloomberg, IMF

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Global Financial Indicators

Last updated: 12/2/20 8:44 AM	Level: Last 12m	Level: Latest	Change: 1 Day	Change: 7 Days	Change: 30 Days	Change: 12 M	YTD
Equities					%		%
United States		3659	1.1	1	11	18	13
Europe		3503	-0.6	0	16	-3	-6
Japan		26801	0.1	2	15	14	13
China		3449	-0.1	3	7	20	13
Asia Ex Japan		86	1.5	0	8	24	17
Emerging Markets		50	2.0	1	10	18	11
Interest Rates					basis points		
US 10y Yield		0.94	1.0	5	9	-88	-98
Germany 10y Yield		-0.52	1.2	5	12	-24	-33
Japan 10y Yield		0.03	0.6	1	-2	7	4
UK 10y Yield		0.35	0.4	3	13	-39	-47
Credit Spreads					basis points		
US Investment Grade		103	-0.4	-4	-25	-13	5
US High Yield		425	-0.4	-8	-103	-41	32
Europe IG		47	0.9	-2	-15	-2	3
Europe HY		253	1.5	-18	-102	27	46
Exchange Rates					%		
USD/Majors		91.33	0.0	-1	-3	-7	-5
EUR/USD		1.21	0.0	1	4	9	8
USD/JPY		104.6	-0.2	0	0	4	4
EM/USD		56.7	-0.1	1	5	-6	-8
Commodities					%		
Brent Crude Oil ($/barrel)		47	-0.3	-3	21	-22	-28
Industrials Metals (index)		132	-0.9	2	10	19	15
Agriculture (index)		43	-0.7	-3	4	9	3
Implied Volatility					%		
VIX Index (%, change in pp)		21.1	0.4	-0.5	-16.0	6.2	7.4
US 10y Swaption Volatility		54.3	2.0	-0.2	-23.4	-8.6	-7.7
Global FX Volatility		7.7	0.0	0.1	-1.3	1.8	1.7
EA Sovereign Spreads					10-Year spread vs. Germany (bps)		
Greece		119	0.7	-6	-38	-61	-46
Italy		119	-1.7	0	-20	-45	-41
Portugal		59	-1.3	0	-14	-15	-4
Spain		63	-1.7	-1	-13	-14	-2

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

back to top

Emerging Market Financial Indicators

Last updated:	Exchange Rates							Local Currency Bond Yields (GBI EM)						
12/2/2020	Level		Change (in %)					Level		Change (in basis points)				
8:46 AM	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		6.56	0.1	0.2	2	7	6		3.4	-1.8	-4	5	16	24
Indonesia		14125	0.0	0.1	4	0	-2		6.2	-3.1	-6	-42	-102	-93
India		74	-0.2	0.2	1	-3	-3		6.0	1.3	1	-4	-82	-90
Philippines		48	0.0	0.2	1	6	5		3.6	-0.1	-3	6	-65	-66
Thailand		30	0.0	0.3	3	0	-1		1.5	0.4	1	-2	-25	-16
Malaysia		4.08	0.0	0.2	2	2	0		2.7	-1.6	12	20	-71	-68
Argentina		81	0.0	-0.8	-3	-26	-27		53.7	7.1	52	334	-3461	-887
Brazil		5.23	-0.1	1.7	10	-19	-23		6.3	-19.0	-37	-16	10	8
Chile		756	0.6	1.9	2	6	-1		2.9	4.0	11	15	-56	-42
Colombia		3555	0.4	1.8	9	-1	-8		5.2	1.7	5	-20	-93	-77
Mexico		20.11	-0.4	-0.7	6	-3	-6		5.8	-2.4	-6	-37	-129	-110
Peru		3.6	-0.1	0.0	0	-6	-8		3.9	2.0	-3	-22	-71	-62
Uruguay		42	-0.2	0.4	1	-11	-12		7.5	-0.4	10	-8	-376	-338
Hungary		296	-0.3	2.2	6	1	0		1.6	0.6	1	-15	50	43
Poland		3.70	-0.5	1.1	7	4	2		0.7	2.4	2	4	-113	-123
Romania		4.0	0.0	1.4	4	7	6		2.9	0.0	3	-16	-119	-109
Russia		75.6	0.3	0.0	7	-15	-18		5.6	0.5	3	-22	-69	-55
South Africa		15.4	-0.8	-1.6	6	-5	-9		9.9	0.8	14	-34	22	38
Turkey		7.85	-0.2	1.1	7	-27	-24		12.5	14.8	20	-173	52	85
US (DXY; 5y UST)		91	0.0	-1.0	-3	-7	-5		0.42	0.3	3	4	-122	-127

	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		5067	0.0	3	7	32	24		207	1	-8	-5	25	31
Indonesia		5814	1.6	2	14	-5	-8		183	0	-7	-38	6	27
India		44618	-0.1	0	12	9	8		164	1	-6	-45	37	39
Philippines		7081	1.0	0	12	-10	-9		107	-2	-4	-22	23	41
Malaysia		1599	-0.2	0	9	2	1		119	-1	-8	-32	-2	7
Argentina		54913	0.6	1	16	64	32		1425	20	47	-42	-977	-344
Brazil		111606	2.3	1	19	2	-3		258	1	-6	-50	18	43
Chile		4092	1.9	-1	15	-9	-12		150	1	-2	-26	1	17
Colombia		1285	2.2	2	13	-20	-23		218	1	-4	-28	29	55
Mexico		42896	2.7	0	16	1	-1		420	1	-4	-62	94	128
Peru		20146	1.8	3	13	1	-2		152	1	-1	1	26	45
Hungary		39022	0.7	0	18	-10	-15		99	1	-3	-9	3	13
Poland		53305	0.7	0	18	-6	-8		5	0	-2	-11	-20	-13
Romania		9345	0.6	2	10	-5	-6		204	-7	-2	-37	10	30
Russia		3169	0.7	1	16	8	4		174	0	-4	-34	15	43
South Africa		58120	1.1	1	10	6	2		408	-2	-10	-75	58	88
Turkey		1322	-0.2	0	17	22	16		489	-5	-22	-157	51	88
Ukraine		508	0.0	1	1	0	0		509	-3	-23	-166	4	89

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

back to top