



- Treasury yields shoot higher on growth optimism, convexity hedging ([link](#))
- US retail sales and producer price inflation in January blow out expectations ([link](#))
- EM local currency bonds and exchange rates fall in sync with global trend ([link](#))
- UK inflation beats expectations ([link](#))
- Profits of S&P 500 firms surpassed pre-pandemic level ([link](#))

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Rising bond yields ripple through global markets

Global yield curve steepening ripped higher yesterday, testing investor sentiment. The sell-off in long-dated bonds accelerated yesterday around the world with help from convexity hedging flows in major markets, sending real US yields and the dollar higher. Risk asset investors reacted cautiously, with global equities cooling (-0.3%), EM currencies and local rates weakening, and traditional inflation hedges like gold plummeting (-8%). Yield curve steepening paused overnight, but appears set to get new momentum this morning after US retail sales and producer price inflation for January blew out expectations. The data followed the passage of stimulus in December and was being widely watched for its implications for how consumers will react to the larger fiscal relief package planned in the Biden administration's upcoming COVID relief package. Further increases in demand and inflation may breathe new life into growth-sensitive risk assets and push government bond yields yet higher, but are likely to provide fodder for those who say the relief package will overheat the economy.

Key Global Financial Indicators

Last updated: 2/17/21 8:11 AM	Level		Change from Market Close				YTD
	Last 12m	Latest	1 Day	7 Days	30 Days	12 M	
Equities			%				%
S&P 500		3933	-0.1	0	4	16	5
Eurostoxx 50		3719	-0.2	2	3	-3	5
Nikkei 225		30292	-0.6	3	6	29	10
MSCI EM		58	0.2	3	7	31	12
Yields and Spreads			bps				
US 10y Yield		1.31	-0.5	19	23	-28	40
Germany 10y Yield		-0.34	0.8	10	20	6	23
EMBIG Sovereign Spread		342	2	0	-15	42	-8
FX / Commodities / Volatility			%				
EM FX vs. USD, (+) = appreciation		57.8	-0.2	0	1	-3	0
Dollar index, (+) = \$ appreciation		90.8	0.4	0	0	-8	1
Brent Crude Oil (\$/barrel)		64.5	1.8	5	17	12	24
VIX Index (% change in pp)		21.2	-0.3	0	-3	7	-2

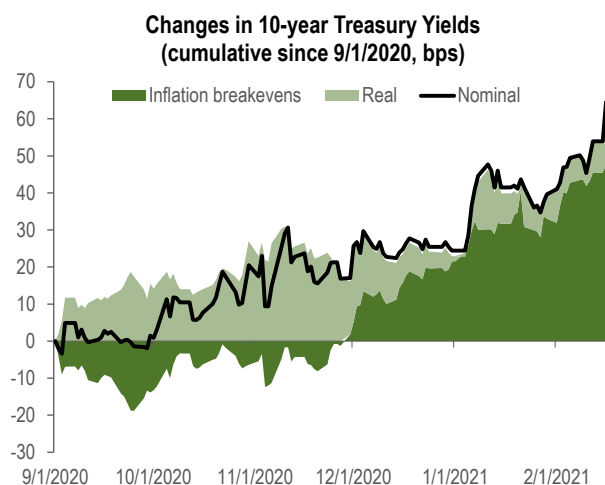
Colors denote **tightening/easing** financial conditions for observations greater than ± 1.5 standard deviations. Data source: Bloomberg.

United States

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Retail sales came in much stronger than expected in January. The headline sales increased 5.3% mom with sales ex-auto and gas up 6.1% mom, compared to 1.1% and 0.8% expected respectively.

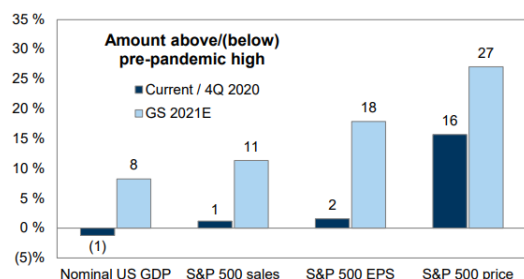
Treasury yields jumped yesterday while stocks briefly touched record highs on continuing optimism for an economic recovery. The Treasury curve steepened sharply with 10-year yield up 9 bps to 1.31% and 30-year yield up 8 bps to 2.09%, both back at the levels last seen in mid-Feb 2020. Today's move was driven by higher real rates, with 10-year TIPS yield up 7 bps to -0.93%, contrary to early February where the expansion in inflation breakevens played a dominant role. The moves were reportedly amplified by convexity hedging flows, e.g. from holders of mortgage backed securities and other investors who seek to reduce duration as interest rates rise. Major stock indices closed slightly lower after briefly touching record highs in the morning session, as the rally in energy (+2.3%) and financial (+1.7%) shares failed to offset the drop in rate-sensitive sectors. In economic news, the Empire Manufacturing Index rose more than expected in February, up 8.6 pts to 12.1. The composition of the report was favorable, with improvements in new orders, employment and expected business conditions. The prices paid measure rose to the highest level since 2011 (+12.3 pts to 57.8) as the shipment component dropped 3.3 pts, due to supply chain disruptions from the winter storm.



The Federal Reserve released scenarios for its 2021 stress tests. The “severely adverse” scenario envisions a global recession beginning in 2021Q1, with substantial stress in commercial real estate and corporate debt market. Capital positions from 19 large banks will be tested against a 4% drop in GDP, 4 ppts increase in unemployment rate, 55% drop in equity prices, 425 bps widening in IG credit spreads and a near 50 pts increase in VIX index. Additional market and credit shocks will be imposed on banks with large trading or processing operations.

S&P 500 constituent firm profits have surpassed their pre-pandemic level. Results from 367 firms accounting for 84% of S&P 500 market cap show that 4Q EPS rose 2% y/y to a record high, while consensus was pointing to a 11% y/y contraction. 65% of S&P 500 firms reported EPS more than one standard deviation above consensus, ranking just behind 2020Q3 as the best quarter in over 2 decades.

Exhibit 1: S&P 500 EPS in 4Q 2020 exceeded the pre-pandemic high by 2%
S&P 500 price as of February 11, 2021; GDP, sales, and EPS as of 4Q 2020



Source: Goldman Sachs Global Investment Research.

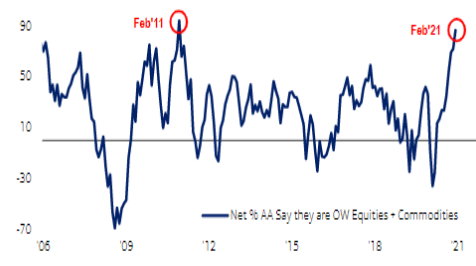
Exhibit 2: Most sectors beat expectations and experienced positive revisions
as of February 11, 2021

Sector	4Q 2020 EPS		Consensus 2021 EPS		
	Year/year growth	% of stocks beating by 1 std. dev.	Growth vs. 2020	Growth vs. 2019	Revision since start of 4Q reports
Materials	17 %	73 %	34 %	26 %	4 %
Info Tech	14	79	13	22	4
Health Care	8	61	13	18	2
Utilities	(1)	33	4	8	0
Consumer Staples	4	56	5	8	1
Comm Services	8	71	12	6	5
Consumer Discretionary	(1)	58	49	5	1
Real Estate	(9)	35	3	2	1
Financials	14	74	23	(5)	4
Industrials	(36)	70	66	(16)	(2)
Energy	(101)	33	NM	(43)	11
S&P 500	2 %	65 %	22 %	5 %	3 %

Source: FactSet, Goldman Sachs Global Investment Research

Investor optimism on reflation trades continues to build. The BofA fund manager survey shows that 87% of fund managers on net are currently overweight equities and commodities in their portfolios, just shy of the previous peak in Feb 2011. Meanwhile, the majority of investors believe the US equity market is in a late-stage bull market, compared to 11% who believe the market is currently in bubble territory. Consequently, fund managers continue to draw down their cash balance, with a record amount of investors taking on higher than normal risks. Failure of vaccine rollout, taper tantrum in bond market and higher than expected inflation remain the top tail risks.

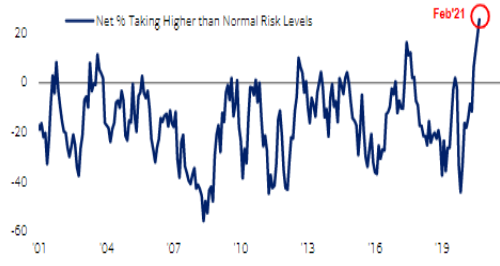
Exhibit 15: FMS Global equity + commodity allocation highest in 10-years
Net % AA Say they are OW Equities + Commodities



Source: BofA Global Fund Manager Survey

BoFA GLOBAL RESEARCH

Exhibit 11: All-time high in investors taking "higher-than-normal" risk
Net % Taking Higher than Normal Risk Levels



Source: BofA Global Fund Manager Survey

BoFA GLOBAL RESEARCH

Europe

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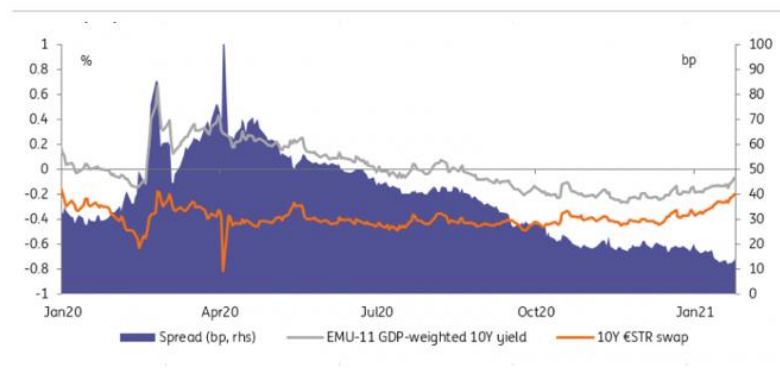
European equities retreated after reaching the highest level since the start of the pandemic. A handful of corporate results out of the consumer goods sector disappointed investors this morning including Germany's Beiersdorf (Nivea), Italy's Kering (Gucci) as well as British American Tobacco. The STOXX 600 benchmark was down 0.4% with only energy (+1.3%) and basic materials (+0.3%) sectors up on broader commodity market gains.

European stocks are falling after climbing to a one-year high this week



European sovereign bond markets were stable this morning with Germany's 10-year bund yields lower 1 bps, after 10 bps gains over the last three days. Much of the sell-side research has been focused on the recent yield-curve dynamics with analysts debating to what extent the rise in European yields is imported from the U.S. as compared to reflecting domestic economic recovery and reflation prospects. With ECB's weekly purchases under the Pandemic Emergency Purchase Program remaining below average, markets participants are increasingly adopting a view that the central bank would not fight the gradual increase in yields. Nevertheless, the **rise in government bond yields has been lagging those of swap rates**, indicating that the asset purchases in place are having a dampening effect on relative yield curve dynamics.

Government yields have risen, but less than swap rates

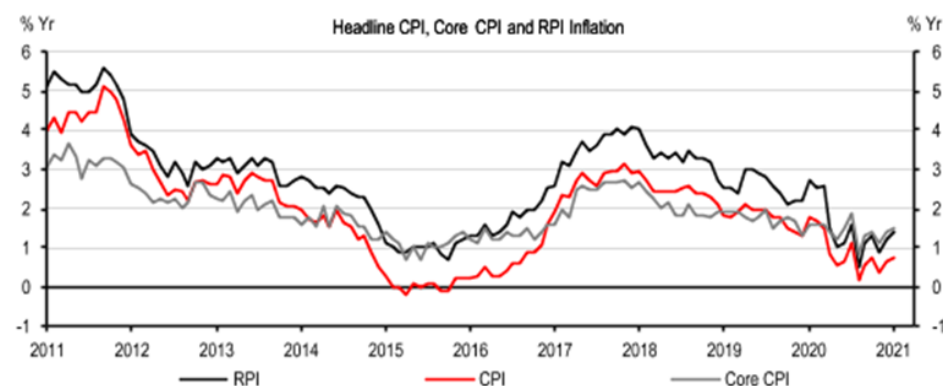


Source: Refinitiv, ING

United Kingdom

Inflation edged up in January to 0.7% y/y with core and RPI measures reaching 1.4%. All three measures came 0.1 ppt above consensus estimates. Most analysts expect an upward path of inflation closer to Bank of England (BOE) 2% target later this year on the back of VAT-cut reversals (April), inflation reweighting (March), Brexit-related import price pressure and broader impact of commodity and in particular oil price increase. **That said, contacts doubt that the inflation increase may be sustained into 2022, which should keep the central bank on the sideline rather than pursuing tightening.** A lack of clarity around the extension of the asset purchase program remains a risk factor and UK's gilt market has been the underperformer among G4. **Long-end bond yields have risen by 30 bps in the last two weeks with contacts pointing to increasingly thin liquidity and poor demand in long-dated bond auctions due to weakening appetite for duration.**

Chart 1: The main inflation rates edged up in January



Source: ONS

Other Mature Markets

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Australia and New Zealand

Government bond yields increased (10-year, New Zealand: + 9 bps and Australia: +8 bps) following a surge in U.S. treasury yields. The Aussie dollar was little changed, while the Kiwi dollar depreciated (-0.2%). **In Australia**, Reserve Bank of Australia (RBA) Assistant Governor Kent said that the Australian dollar would be as much as 5% stronger without a QE program, on the back of favorable commodity prices. The RBA earlier this month extended its bond-buying program by AUD 100 bn (\$77.4 bn) over six months.

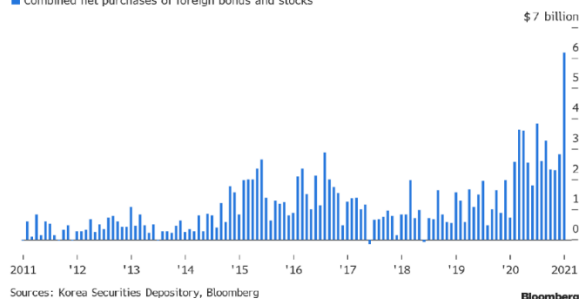
Korea

The won underperformed on outflows from both local and foreign investors. In 2021, the won is among the worst performers in the region after depreciating 2% year-to-date. The weakness of Korean won is an anomaly—risk appetite is picking up, but the currency is weakening. Fund outflows are said to be the main driver. Domestic investors bought a net \$6.2 bn of overseas bonds and stocks in January, while foreign investors offloaded a net \$5.3 bn of local stocks in the last week of January. **The won depreciated (-0.7%); equities fell (-0.9%); and government bond yields increased (10-year: +1.7 bps).**

Bye Bye Seoul

South Korean investors bought a record amount of foreign assets in January

■ Combined net purchases of foreign bonds and stocks



Source: Bloomberg.

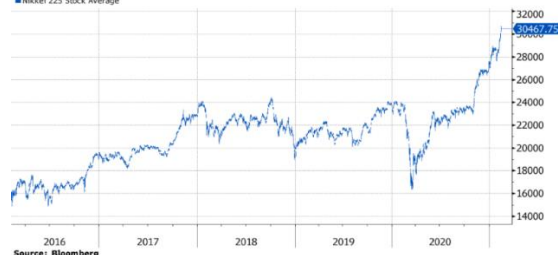
Japan

Bank of Japan (BOJ) Governor Kuroda said that ETF purchases are still needed as part of large-scale monetary easing. As share prices rise to a post-1990 record high, the BOJ is facing public criticism that the BOJ has inflated a stock market bubble. The BOJ is currently the largest single owner of Japanese shares after a years-long buying program. Governor Kuroda said that current share prices probably reflect the outlook for corporate profits, better-than-expected economic performance, and the vaccine rollout. He noted that the BOJ is conducting ETF purchases in a flexible manner and does not aim at any specific price level. Governor Kuroda also said that it will be difficult to attain the inflation target in 2023. **Prime Minister Suga similarly defended the BOJ's ETF purchases. Equities declined (Nikkei: -0.6%) in line with the regional trend; the yen appreciated (+0.1%); and government bond yields increased (10-year: +1.6 bps; 30-year: +1.1 bps).**

Growing Optimism

Japan's benchmark stock index has risen to the highest level since 1990

■ Nikkei 225 Stock Average



Emerging Markets [back to top](#)

Most Asian stock markets declined, led by Philippine (-1.1%), Indonesia (-1.0%) and Korean (-0.9%) equities. Share prices rose in Taiwan POC (+3.5%) and Hong Kong SAR (+1.1%), driving up MSCI's emerging Asia index (+0.8%). **Asian currencies depreciated**, led by Korean won (-0.7%) and Indonesian rupiah (-0.6%). Offshore RMB depreciated (-0.3%), while the onshore market remains closed for the holidays. **Long-end government bond yields increased** (for 10-year, Indonesia: +17.4 bps, Singapore: +11.9 bps). A surge in U.S. treasury yields (10-year surpassing 1.3%) weighed on sentiment, putting pressures on Asian currencies and government bond yields. **In Indonesia**, pressures emerged after the government sold 30 tn rupiah (\$2.14 bn) of treasury bills and bonds, below the 35 tn rupiah (\$2.5 bn) target, despite the auction being over-subscribed. The share of foreign purchases dropped to 14.1% from 18.7%.

In EMEA, markets traded with a cautious tone after U.S. 10-yr rates rose to 1.30% yesterday. Currencies are generally weaker, led by the South African rand (-0.9%). The Nigerian naira fell 7% in the spot market as contacts believe that the central bank may struggle to contain inflationary pressures after headline inflation accelerated to 16.5% yoy in January. Equities were mixed.

Latin American stock markets rallied, currencies depreciated, and sovereign yields rose. Equities rallied in Peru (+1.6%), Mexico (+1.2%) and Chile (+0.7%), with the expected start of vaccinations supporting the investor mood, while stocks retreated in Colombia (-0.5%). Currencies depreciated in Mexico (-0.9%) and Colombia (-0.6%) and stood virtually unchanged in Peru and Chile. Stalling oil prices weighed on the Colombian and Mexican peso, with the latter weakening on news that wearther related energy production interruptions could generate \$2.7 bn of revenue losses. Markets in Brazil and Argentina remained closed on Carnival. The continued steepening of the US treasury yield curve pushed longer term sovereign yields in the region up, with 10-year yields of hard-currency sovereign debt up by 9 to 12 bps and respective local currency debt increasing from 0.4 bps in Chile to 11 bps in Mexico.

Key Emerging Market Financial Indicators

Last updated: 2/17/21 8:13 AM	Level		Change				
	Last 12m	index	1 Day	7 Days	30 Days	12 M	YTD
Major EM Benchmarks			%				%
MSCI EM Equities		57.94	0.4	3	7	31	12
MSCI Frontier Equities		29.94	1.4	3	1	-1	6
EMBIG Sovereign Spread (in bps)		342	2	0	-15	42	-8
EM FX vs. USD		57.83	-0.2	0	1	-3	0
Major EM FX vs. USD			%, (+) = EM currency appreciation				
China Renminbi		6.46	-0.4	0	0	8	1
Indonesian Rupiah		14020	-0.6	0	0	-3	0
Indian Rupee		72.75	-0.1	0	1	-2	0
Argentine Peso		88.82	-0.3	-1	-3	-31	-5
Brazil Real		5.37	0.1	0	-1	-19	-3
Mexican Peso		20.31	-0.7	-1	-3	-9	-2
Russian Ruble		73.87	-0.3	0	0	-14	0
South African Rand		14.78	-0.8	0	3	1	-1
Turkish Lira		6.99	-0.1	1	7	-14	6
EM FX volatility		9.61	0.0	-0.1	-0.8	3.2	-1.1

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

India

The Reserve Bank of India (RBI) is managing to keep government bond yields in check, but other sectors see rising borrowing costs. Larger-than-expected government borrowing pushed up bond yields days after the budget. The RBI has stepped in, with large-scale open market operations helping hold the 10-year bond yield at around 6%. However, borrowing costs in other sectors have risen. For example, spreads of state bond yields further widened. Extra yields offered by state bonds increased to 91-106 bps this week, compared with 72-86 bps two weeks ago. In the corporate bond market, there is hardly any appetite for AA- and A-rated corporate papers that are traded at limited yield spreads (up to 300 bps). **The rupee depreciated (-0.2%); equities declined (-0.8%); and government bond yields rose slightly (10-year: +0.7 bp)**

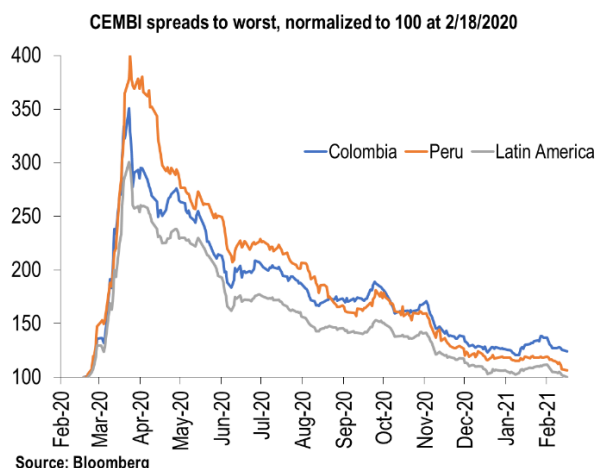
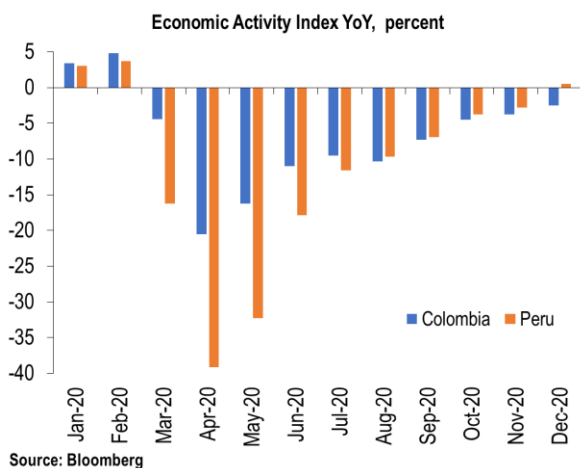
Rising State Bond Yields

Yields of state bonds have risen sharply this month



Peru and Colombia

Growth prints beat expectations in Andean economies, but investors focused on vaccinations and terms of trade boost. December's economic activity growth in Peru and Colombia printed on Monday 0.5% and -2.5% yoy, higher than expected (-1.7% and -4% respectively) and up from -2.8% and -3.4% the month before. Analysts point out that the country's recovery remains uneven with construction and mining suffering from lower investment and a decrease in net exports in the fourth quarter of 2020 adding to this drag, but also see that vaccinations and improved terms of trade are expected to deliver an additional boost in the near term. Market reactions have been muted but equities rose in Peru on news that mass vaccination will start on Wednesday. Corporate credit costs in both countries are nearing pre-Covid-19 levels.





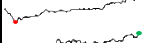
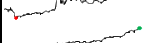

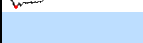


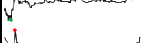




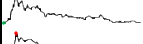








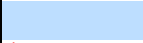



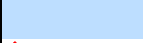
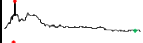

List of GMM Contributors

Global Markets Analysis Division, MCM Department

Nassira Abbas <i>Deputy Division Chief</i>	Dimitris Drakopoulos <i>Financial Sector Expert</i>	Dmitri Petrov <i>Financial Sector Expert</i>
Antonio Garcia-Pascual <i>Deputy Division Chief</i>	Deepali Gautam <i>Research Officer</i>	Thomas Piontek <i>Financial Sector Expert</i>
Evan Papageorgiou <i>Deputy Division Chief</i>	Rohit Goel <i>Financial Sector Expert</i>	Patrick Schneider <i>Research Officer</i>
Jose Abad <i>Financial Sector Expert</i>	Sanjay Hazarika <i>Senior Financial Sector Expert</i>	Can Sever <i>Economist</i>
Sergei Antoshin <i>Senior Economist</i>	Frank Hespeler <i>Senior Financial Sector Expert</i>	Juan Solé <i>Senior London Representative</i>
John Caparusso <i>Senior Financial Sector Expert</i>	Henry Hoyle <i>Financial Sector Expert</i>	Jeffrey Williams <i>Senior Financial Sector Expert</i>
Yingyuan Chen <i>Financial Sector Expert</i>	Mohamed Jaber <i>Senior Financial Sector Expert</i>	Dmitry Yakovlev <i>Senior Research Officer</i>
Han Teng Chua <i>Economic Analyst</i>	Phakawa Jeasakul <i>Senior Economist</i>	Akihiko Yokoyama <i>Senior Financial Sector Expert</i>
Fabio Cortés <i>Senior Economist</i>	Sonia Meskin <i>Financial Sector Expert</i>	Xingmi Zheng <i>Research Assistant</i>
Reinout De Bock <i>Economist</i>	Natalia Novikova <i>IMF Resident Representative in Singapore</i>	

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Global Financial Indicators

Last updated: 2/17/21 8:09 AM	Level		Change				YTD
	Last 12m	Latest	1 Day	7 Days	30 Days	12 M	
Equities			%				%
United States		3929	0.2	0	4	16	5
Europe		3718	-0.2	2	3	-3	5
Japan		30292	-0.6	3	6	29	10
China		3655	1.4	4	3	26	5
Asia Ex Japan		102	0.1	3	7	39	14
Emerging Markets		58	0.2	3	7	31	12
Interest Rates			basis points				
US 10y Yield		1.31	-0.8	18	22	-28	39
Germany 10y Yield		-0.34	0.6	10	20	6	23
Japan 10y Yield		0.10	1.4	2	6	13	8
UK 10y Yield		0.62	0.3	14	34	-2	43
Credit Spreads			basis points				
US Investment Grade		86	0.1	-4	-9	-20	-9
US High Yield		343	1.0	-10	-30	-70	-36
Europe IG		48	0.3	0	-4	6	0
Europe HY		245	1.4	2	-14	34	2
EMBIG Sovereign Spread		342	2.2	0	-15	42	-8
Exchange Rates			%				
USD/Majors		90.81	0.3	0	0	-8	1
EUR/USD		1.21	-0.4	0	0	11	-1
USD/JPY		106.1	0.0	1	2	-3	3
EM/USD		57.8	-0.2	0	1	-3	0
Commodities			%				
Brent Crude Oil (\$/barrel)		64	1.8	5	17	12	24
Industrials Metals (index)		142	0.1	3	5	33	7
Agriculture (index)		51	-0.3	0	0	30	7
Implied Volatility			%				
VIX Index (% change in pp)		21.2	-0.3	-0.5	-3.2	7.5	-1.6
US 10y Swaption Volatility		75.4	2.1	15.4	17.2	9.7	15.3
Global FX Volatility		7.3	0.0	0.1	-0.5	1.9	-0.8
EA Sovereign Spreads			10-Year spread vs. Germany (bps)				
Greece		116	3.5	-7	-5	-19	-4
Italy		93	0.9	-1	-23	-38	-18
Portugal		54	0.7	2	0	-15	-6
Spain		65	0.4	6	4	-4	3

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: 2/17/2021 8:13 AM	Exchange Rates							Local Currency Bond Yields (GBI EM)							
	Level		Change (in %)					YTD	Level		Change (in basis points)				YTD
	Last 12m	Latest	1 Day	7 Days	30 Days	12 M	Last 12m		Latest	1 Day	7 Days	30 Days	12 M		
	vs. USD		(+) = EM appreciation						% p.a.						
China		6.46	-0.4	0.1	0	8	1		3.3	0.0	-1	7	44	6	
Indonesia		14020	-0.6	-0.3	0	-3	0		6.3	2.3	3	0	-41	20	
India		73	-0.1	0.1	1	-2	0		6.3	1.4	0	26	-29	34	
Philippines		48	-0.3	-0.7	-1	5	-1		3.5	-0.2	-1	-13	-64	-16	
Thailand		30	-0.1	-0.3	0	4	0		1.5	-0.2	8	10	14	19	
Malaysia		4.04	-0.2	0.2	0	3	0		2.8	5.3	10	29	-5	28	
Argentina		89	-0.3	-0.5	-3	-31	-5		44.7	0.0	-455	-726	-1507	-1142	
Brazil		5.37	0.1	0.3	-1	-19	-3		6.5	0.0	5	17	74	94	
Chile		721	-0.4	0.7	2	10	-1		2.8	6.6	7	3	-72	7	
Colombia		3540	-0.6	0.6	-2	-4	-3		5.2	6.2	6	10	-32	11	
Mexico		20.31	-0.7	-1.3	-3	-9	-2		5.7	7.5	4	8	-92	12	
Peru		3.7	-0.2	-0.4	-1	-8	-1		3.9	8.8	11	20	-33	32	
Uruguay		43	0.0	-0.2	0	-11	-1		7.1	-0.1	-6	-15	-280	-18	
Hungary		298	-0.5	-1.1	0	4	0		1.8	3.8	13	15	16	25	
Poland		3.73	-0.5	-0.7	1	5	0		0.8	3.0	12	21	-116	15	
Romania		4.0	-0.4	-0.5	0	9	-2		2.4	6.0	14	-10	-117	-32	
Russia		73.9	-0.3	0.0	0	-14	0		6.3	9.9	36	47	50	61	
South Africa		14.8	-0.8	-0.2	3	1	-1		9.5	10.5	3	-23	10	-11	
Turkey		6.99	-0.1	1.0	7	-14	6		13.4	11.6	9	-15	220	30	
US (DXY; 5y UST)		91	0.4	0.4	0	-8	1		0.58	0.3	13	13	-84	22	

	Equity Markets							Bond Spreads on USD Debt (EMBIG)						
	Level		Change (in %)				YTD	Level		Change (in basis points)				YTD
	Last 12m	Latest	1 Day	7 Days	30 Days	12 M		Last 12m	Latest	1 Day	7 Days	30 Days	12 M	
								basis points						
China		5808	0.0	6	7	47	11		199	0	-2	-9	30	-9
Indonesia		6228	-1.0	1	-2	6	4		158	0	-9	-25	-5	-29
India		51704	-0.8	1	5	26	8		152	-3	-3	-6	20	1
Philippines		6966	-1.1	-1	-4	-5	-2		83	0	-9	-17	13	-22
Malaysia		1595	-0.7	1	-2	4	-2		113	0	-2	-3	9	3
Argentina		51466	0.0	1	2	33	0		1459	0	19	8	-570	91
Brazil		119429	0.0	0	-1	4	0		253	0	0	-16	58	3
Chile		4641	0.7	3	2	0	11		126	0	-6	-16	-14	-18
Colombia		1363	-0.5	-1	-6	-18	-5		207	0	-4	-15	44	2
Mexico		44699	1.2	-1	-3	-1	1		348	0	-9	-34	55	-12
Peru		22597	1.6	1	5	14	9		133	0	-4	-3	22	1
Hungary		44978	0.1	2	2	-1	7		65	0	-6	-15	-42	-31
Poland		59396	0.0	5	3	2	4		-22	0	-4	-11	-54	-21
Romania		10478	-0.5	-1	3	4	7		191	4	0	-12	16	-12
Russia		3493	-0.1	3	1	12	6		159	0	-5	-3	19	-7
South Africa		67332	0.2	2	6	16	13		357	0	-4	-35	25	-23
Turkey		1543	0.0	0	1	28	4		421	0	-5	-47	34	-24
Ukraine		521	0.0	0	4	-1	4		479	0	12	-21	127	-12
EM total		58	0.4	3	7	31	12		421	0	17	-10	97	128

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

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