Global Markets Monitor

TUESDAY, FEBRUARY 2, 2021

- **Bond markets highly vulnerable to interest rate shocks** (link)
- **Low volatility has kept US bond yields contained so far** (link)
- **Euro area Q4 GDP contracts less than expected** (link)
- **Reserve Bank of Australia surprises by increasing QE program** (link)
- **Ethiopia to review debt under G-20 Common Framework** (link)

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

Global markets extend February rebound

Optimism prevailed for a second day as markets extended Monday's strong gains in global risk assets. Several markets are back in positive territory for the year after falling into the red last week. Declining infection counts and hopes for a large new fiscal stimulus pushed US markets higher, with futures markets pointing to further gains. The disruptions in China's money markets are fading away, while the euro area's latest GDP was ahead of forecasts. Corporate earnings in the US and Europe continue to exceed expectations. Crude oil is at a one-year high. The Reserve Bank of Australia boosted markets by unexpectedly increasing its quantitative easing program, the latest in a series of positive macro surprises on the policy front. Treasury and bund yields are higher as safe haven flows recede. Nevertheless, multiple challenges remain as countries struggle with the vaccine rollout and new mutant strains of the virus complicate recovery efforts. February may emerge as a watershed month in the global struggle against the pandemic.

Key Global Financial Indicators

Last updated: 2/2/21 8:04 AM	Level		Change from Market Close				
	Last 12m	Latest	1 Day	7 Days	30 Days	12 M	YTD
Equities					%		%
S&P 500		3774	1.6	-2	0	17	0
Eurostoxx 50		3578	1.3	0	1	-2	1
Nikkei 225		28362	1.0	-1	3	22	3
MSCI EM		55	2.7	-3	6	30	6
Yields and Spreads					bps		
US 10y Yield		1.12	3.6	8	20	-39	20
Germany 10y Yield		-0.48	3.3	5	9	-5	9
EMBIG Sovereign Spread		352	1	-6	1	38	1
FX / Commodities / Volatility					%		
EM FX vs. USD, (+) = appreciation		57.4	0.1	0	-1	-4	-1
Dollar index, (+) = $ appreciation		91.2	0.2	1	1	-6	1
Brent Crude Oil ($/barrel)		57.6	2.3	3	11	-1	11
VIX Index (%, change in pp)		27.7	-2.6	5	5	9	5

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

United States

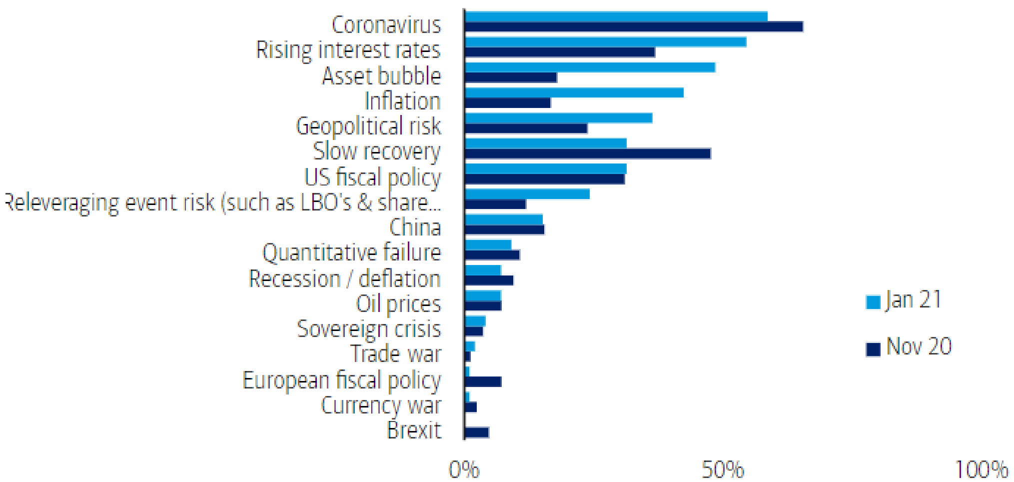
back to top

Market sentiment in February continued to improve. The US Congressional Budget Office predicted that that US GDP will regain its pre-pandemic level in the second half of this year, although the damage to employment could linger into 2024 (the estimate excluded the stimulus package currently under discussion). Following the meeting on stimulus measures between the President and ten Republican senators, markets are leaning towards the view that the administration is likely to go with a larger package using the budget reconciliation process. Dallas Fed President Kaplan was surprisingly optimistic about the economy, while making it clear that he agreed with Fed Chair Powell's statement that talk of tapering was "premature." Meanwhile, earnings season continues with today's calendar featuring Amazon, Google, Exxon and Pfizer, among others

Rising interest rates have emerged as a major worry for investors even as the virus continues to top the table of key risks in the latest Bank of America investor survey. Concerns about an asset bubble have also grown in prominence. Bond markets are at very high risk from an interest rate shock, as bonds issued over the past couple of years have very low coupons due to the historically low level of interest rates. Low coupon bonds are more much sensitive than high coupon bonds to a sudden increase in interest rates. Bank of America thinks interest rates will rise gradually though the year, with the benchmark 10-year Treasury yield hitting 1.75% by the end of the year. A gradual rise will keep bond prices in check as investors are able to adjust their portfolios, but a sudden shock could prove to be highly destabilizing.

Figure 17: Credit investors: What are your biggest concerns?

US credit investors indicated in our recent survey that Coronavirus is the biggest concern, followed by Rising interest rates, Asset bubble and Inflation.

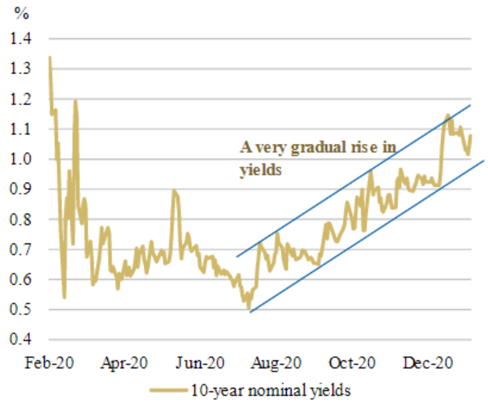


Source: BofA Global Research Credit Investor Survey

BofA GLOBAL RESEARCH

Despite the concern about rising rates, recent history shows that interest rates have been remarkably stable coming out of the worst of the COVID-19 market shock. The expectation of Fed action if rates get out of hand appears to have kept a lid on interest rates so far. Morgan Stanley shows that markets have been so stable that investors were able to make money from selling interest rate volatility (i.e. betting rate increased will remain orderly and limited) in the derivatives market. Investors have sold options in the swaption market (swaptions are options on interest rate swap market). This is highly unusual because interest rate volatility usually goes up as rates rise.

Exhibit 13: Move in 10y nominals over the last nine months



Source: Bloomberg, Morgan Stanley Research

Exhibit 14: PnL from selling 1m and 3m straddles (delta hedged) over the last six months

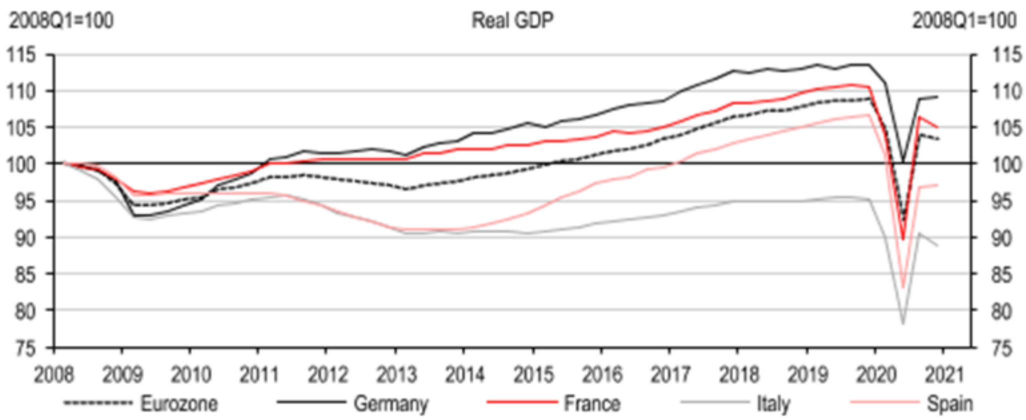
Source: Bloomberg, Morgan Stanley Research

Europe

back to top

Eurozone GDP contracted less than expected in Q4. According to preliminary estimates, the economy contracted 0.7% qoq (-0.9% revised consensus) bringing the yoy decline to 5.1%. Market reaction was somewhat muted as investors already priced in improved growth dynamics following better data out of France and Spain last week. Further on the country level, Italy's GDP came in line with consensus (-2% qoq) while Portugal's Q4 GDP unexpectedly expanded (+0.4% vs -2% consensus).

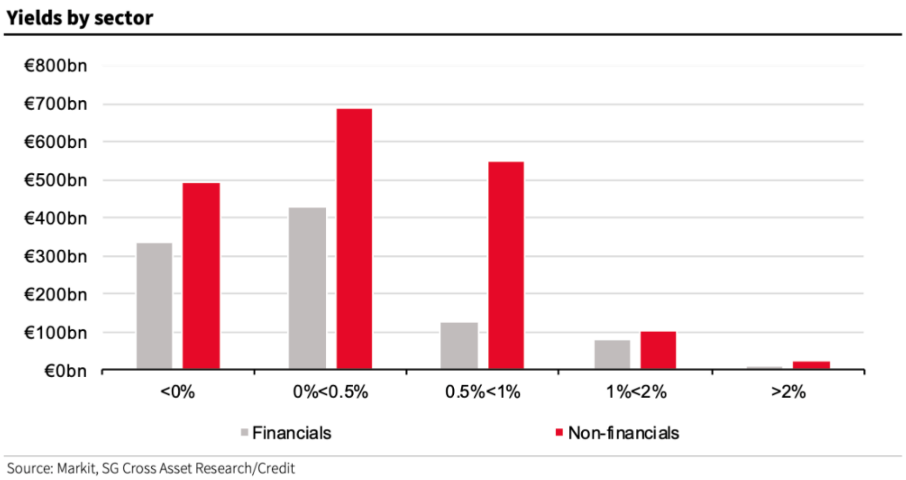
Chart 1: France and Spain posted particularly large upside surprises



Source: Refinitiv Datastream, HSBC

European equity benchmarks extended their recovery with many country indices up 1-1.5%. Sectors such as automobiles (+2.2%), travel and leisure services (+2.2%) and financials (+1.7%) outperformed, indicating easing of vaccine-shortage concerns.

European government bond yields were higher while sovereign spreads unchanged. Corporate credit spread benchmarks tightened for the second day for both investment grade (- 2bps) and high yield (-6 bps) debt. Some analysts highlight that both tight level of spreads as well record low level of absolute yield is likely to put a break on corporate credit performance in Europe. There are now more than €800 bn worth of corporate bonds trading at negative yield with only €200 bn offering yields above 1%.



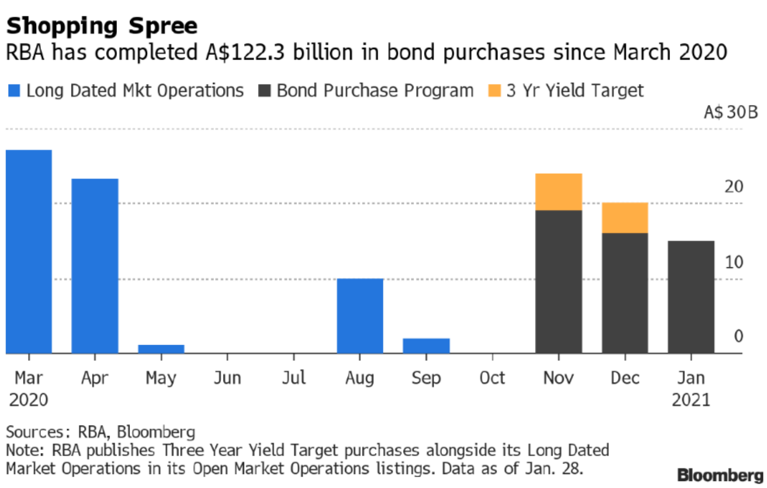
The euro (-0.2%) was approaching the 1.20 mark against the dollar while the sterling (+0.2%) continued to outperform as market participants highlight vaccination-pace relative value trade between the two pairs as the UK continues to outstrip the euro area.

Other Mature Markets

back to top

Australia

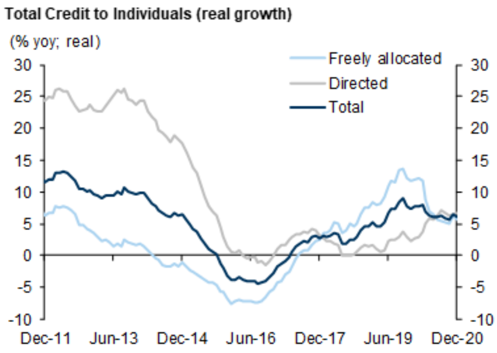
The Reserve Bank of Australia (RBA) surprised markets and unexpectedly increased its QE program. While keeping its policy rate and the 3-year government bond yield target unchanged as expected at 0.1, the RBA announced that it will purchase an additional 100 bn Australian dollar ($76.1 bn) of government bonds when its current bond purchase program is completed in mid-April. The RBA also said that it will not increase the policy rate until actual inflation is sustainably within 2%-3% target range, a condition it does not expect to be met until 2024 at the earliest. The market response was noticeable, with the Aussie dollar selling off and stocks staging a noticeable rally.



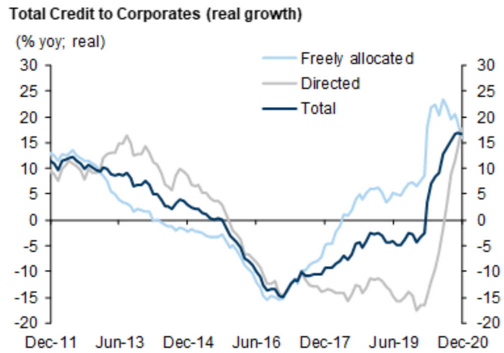
Emerging Markets

back to top

Most markets joined in or extended yesterday's global rally. India stood out with a two-day rally of 7.5% after Monday's announcement of a more aggressive fiscal stimulus for the economy. Geopolitical tensions between the west and Russia remain in focus but Russian equities (+1.6%) and the ruble (+0.5%) gained after data show that Russia's GDP contracted by a less-than-expected 3.1% in 2020 (vs. the 3.7% consensus forecast). The central bank of Ghana left rates unchanged yesterday while warning that a second wave of COVID-19 is making a sharp fiscal recovery in 2021 unlikely. In Brazil, credit conditions remain highly positive for consumers and corporations.



Source: BCB, Goldman Sachs Global Investment Research



Source: BCB, Goldman Sachs Global Investment Research

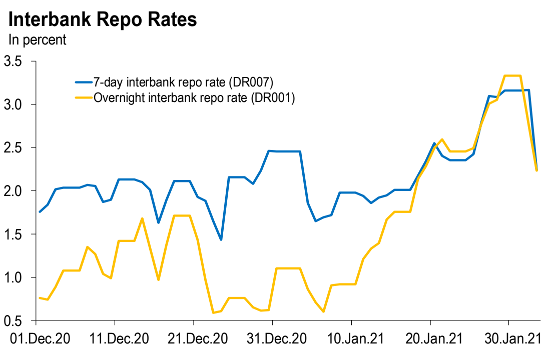
Key Emerging Market Financial Indicators

Last updated:	Level		Change				
2/2/21 8:06 AM	Last 12m	index	1 Day	7 Days	30 Days	12 M	YTD
Major EM Benchmarks					%		%
MSCI EM Equities		54.75	2.0	-3	6	30	6
MSCI Frontier Equities		29.26	1.0	-1	3	-4	3
EMBIG Sovereign Spread (in bps)		352	1	-6	1	38	1
EM FX vs. USD		57.36	0.1	0	-1	-4	-1
Major EM FX vs. USD				**%, (+) = EM currency appreciation**			
China Renminbi		6.46	0.2	0	0	9	1
Indonesian Rupiah		14025	0.0	0	-1	-2	0
Indian Rupee		72.97	0.1	0	0	-2	0
Argentine Peso		87.69	-0.1	-1	-3	-31	-4
Brazil Real		5.41	0.7	-1	-2	-21	-4
Mexican Peso		20.24	0.7	-1	-1	-7	-2
Russian Ruble		75.62	0.8	-1	-2	-16	-2
South African Rand		14.97	0.6	1	-2	-1	-2
Turkish Lira		7.18	0.2	2	3	-17	4
EM FX volatility		10.42	0.0	0.1	-0.3	3.6	-0.3

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

China

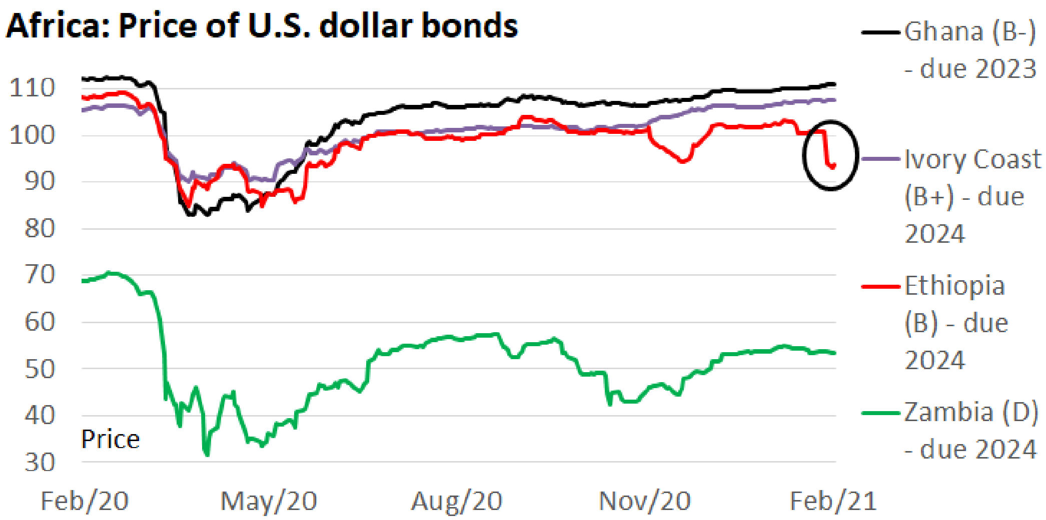
Liquidity stress in the interbank market appeared to ease. The People's Bank of China (PBOC) injected more liquidity today, amounting to 78 bn yuan ($12.1 bn) via open market operations. Interbank repo rates have declined, with the 7-day repo rate (DR007) falling to 2.24% which is close to the PBOC's policy rate target (at 2.2%). Overnight repo rate (DR001) also fell.



Source: Bloomberg.

Ethiopia

Ethiopia is to review its debt under the G-20 Common Framework with a view towards potential restructuring. Ethiopia's Eurobond due 2024 fell 7 points on Friday after Bloomberg reported that the finance ministry will seek to restructure Ethiopia's external debt under the G-20's Common Framework. Contacts do not expect a quick recovery in the price of the Eurobond until there is more clarity on how any potential debt restructuring will proceed. Yesterday, the finance ministry said that the possible restructuring will address the debt vulnerabilities of the country, while preserving long-term access to international financial markets. Ethiopia has a total outstanding Eurobond stock of $1 bn, all due in 2024, and is currently rated B2/B/B by Moody's/Fitch/S&P (all with negative outlooks). Ethiopia is the second African country after Chad to review debt under the Common Framework. **Contacts believe that spillovers have been limited aside from yesterday's price drop of 5 points in Cameroon's Eurobond (rated B2/B-/B) due 2025.**



Source: Bloomberg and IMF

List of GMM Contributors

Global Markets Analysis Division, MCM Department

Nassira Abbas
Deputy Division Chief

Antonio Garcia-Pascual
Deputy Division Chief

Evan Papageorgiou
Deputy Division Chief

Jose Abad
Financial Sector Expert

Sergei Antoshin
Senior Economist

John Caparusso
Senior Financial Sector Expert

Yingyuan Chen
Financial Sector Expert

Han Teng Chua
Economic Analyst

Fabio Cortés
Senior Economist

Reinout De Bock
Economist

Dimitris Drakopoulos
Financial Sector Expert

Deepali Gautam
Research Officer

Rohit Goel
Financial Sector Expert

Sanjay Hazarika
Senior Financial Sector Expert

Frank Hespeler
Senior Financial Sector Expert

Henry Hoyle
Financial Sector Expert

Mohamed Jaber
Senior Financial Sector Expert

Phakawa Jeasakul
Senior Economist

Sonia Meskin
Financial Sector Expert

Natalia Novikova
IMF Resident Representative in Singapore

Dmitri Petrov
Financial Sector Expert

Thomas Piontek
Financial Sector Expert

Patrick Schneider
Research Officer

Can Sever
Economist

Juan Solé
Senior Economist

Jeffrey Williams
Senior Financial Sector Expert

Dmitry Yakovlev
Senior Research Officer

Akihiko Yokoyama
Senior Financial Sector Expert

Xingmi Zheng
Research Assistant

Global Financial Indicators

Last updated: 2/2/21 8:05 AM	Level: Last 12m	Level: Latest	Change: 1 Day	Change: 7 Days	Change: 30 Days	Change: 12 M	YTD
Equities					%		%
United States		3786	1.6	-2	1	17	1
Europe		3578	1.3	0	1	-2	1
Japan		28362	1.0	-1	3	22	3
China		3534	0.8	-1	2	19	2
Asia Ex Japan		96	3.0	-3	7	40	7
Emerging Markets		55	2.7	-3	6	30	6
Interest Rates					basis points		
US 10y Yield		1.12	3.6	8	20	-39	20
Germany 10y Yield		-0.48	3.3	5	9	-5	9
Japan 10y Yield		0.05	-0.5	2	3	12	3
UK 10y Yield		0.36	3.9	10	16	-16	16
Credit Spreads					basis points		
US Investment Grade		95	-0.6	0	0	-15	0
US High Yield		373	-3.5	0	-7	-73	-7
Europe IG		50	-1.2	0	2	5	3
Europe HY		261	-5.6	1	12	33	20
EMBIG Sovereign Spread		352	1.0	-6	1	38	1
Exchange Rates					%		
USD/Majors		91.15	0.2	1	1	-6	1
EUR/USD		1.20	-0.2	-1	-2	9	-1
USD/JPY		105.1	-0.1	-1	-2	3	-2
EM/USD		57.4	0.1	0	-1	-4	-1
Commodities					%		
Brent Crude Oil ($/barrel)		58	2.3	3	11	-1	11
Industrials Metals (index)		132	-0.4	-3	-1	25	-1
Agriculture (index)		50	-0.8	0	4	28	4
Implied Volatility					%		
VIX Index (%, change in pp)		27.7	-2.6	4.6	4.9	8.8	4.9
US 10y Swaption Volatility		59.7	-0.1	5.3	-3.0	-17.5	-0.4
Global FX Volatility		7.7	0.0	0.2	-0.4	1.9	-0.4
EA Sovereign Spreads					10-Year spread vs. Germany (bps)		
Greece		115	-3.7	-7	-5	-46	-5
Italy		113	-1.1	-5	1	-24	1
Portugal		54	-1.3	-2	-6	-16	-6
Spain		60	-1.4	-1	-2	-7	-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)						
2/2/2021	Level		Change (in %)					Level		Change (in basis points)				
8:08 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		6.46	0.2	0.1	0	9	1		3.3	-1.4	5	4	28	4
Indonesia		14025	0.0	0.3	-1	-2	0		6.2	-5.0	-14	12	-72	12
India		73	0.1	0.0	0	-2	0		6.2	9.9	11	21	-70	21
Philippines		48	0.0	0.1	0	6	0		3.6	-5.0	-6	-10	-59	-10
Thailand		30	0.0	-0.1	0	4	0		1.4	2.2	0	5	-11	5
Malaysia		4.05	-0.1	0.0	-1	2	-1		2.7	0.0	8	10	-48	10
Argentina		88	-0.1	-0.8	-3	-31	-4		50.0	21.7	-163	-610	-828	-610
Brazil		5.41	0.7	-1.0	-2	-21	-4		6.3	2.1	-34	72	27	72
Chile		735	0.2	-0.3	-4	7	-3		2.8	1.2	0	1	-65	1
Colombia		3571	0.0	1.1	-3	-5	-4		5.1	3.2	0	7	-44	7
Mexico		20.24	0.7	-1.3	-1	-7	-2		5.6	0.0	1	3	-109	3
Peru		3.6	-0.1	0.1	-1	-7	-1		3.8	2.4	-2	18	-56	18
Uruguay		42	0.0	-0.5	0	-11	0		7.2	-1.1	1	-3	-314	-3
Hungary		295	-0.1	0.0	0	3	0		1.6	0.6	5	8	34	8
Poland		3.74	0.1	0.0	0	4	0		0.6	0.1	3	-4	-129	-4
Romania		4.0	-0.2	-1.0	-2	7	-2		2.3	1.0	-6	-45	-157	-45
Russia		75.6	0.8	-0.6	-2	-16	-2		6.0	-1.5	-2	24	-5	24
South Africa		15.0	0.6	0.6	-2	-1	-2		9.6	-9.9	-13	-10	9	-10
Turkey		7.18	0.2	2.4	3	-17	4		13.3	-3.8	-5	16	334	16
US (DXY; 5y UST)		91	0.2	1.1	1	-6	1		0.44	1.7	3	8	-87	8

	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		5501	1.5	0	6	37	6		204	-2	2	-5	33	-4
Indonesia		6044	-0.4	-2	1	2	1		173	-4	-6	-14	-10	-14
India		49798	2.5	3	4	25	4		157	1	2	6	21	6
Philippines		6868	0.8	-2	-4	-5	-4		96	-3	-1	-8	15	-9
Malaysia		1580	0.9	-1	-3	3	-3		116	0	2	6	4	6
Argentina		49577	2.7	4	-3	24	-3		1446	1	8	77	-645	78
Brazil		117518	2.1	1	-1	3	-1		262	-4	-16	12	38	12
Chile		4414	2.2	-2	6	-3	6		135	-1	-9	-9	-15	-9
Colombia		1357	0.7	-3	-6	-16	-6		216	-2	-8	11	41	11
Mexico		42986	0.0	-4	-2	-3	-2		376	-2	-9	16	66	16
Peru		21610	2.4	1	4	9	4		131	1	-2	-1	8	-1
Hungary		43849	0.3	1	4	2	4		78	0	-5	-18	-39	-18
Poland		57198	-0.5	-1	0	1	0		-14	0	-2	-12	-59	-13
Romania		10423	0.3	1	6	4	6		200	1	-6	-3	6	-3
Russia		3354	1.9	-1	2	9	2		166	1	-7	0	15	0
South Africa		62713	-0.1	-2	6	12	6		383	-2	-10	3	31	3
Turkey		1506	0.9	-2	2	26	2		437	-2	-22	-8	67	-8
Ukraine		521	0.0	1	4	2	4		500	-10	6	9	98	9
EM total		55	2.0	-3	6	30	6		421	0	17	-10	97	128

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