Global Markets Monitor

Monetary and Capital Markets Department
Global Markets Analysis Division

Thursday, February 21, 2019

- **FOMC minutes signal patience on policy rate adjustments and end to balance sheet normalization by year-end ([link](#))**
- **Three UK Conservative MPs resign to join the new Independent party ([link](#))**
- **South African budget proposal to help stabilize ailing public utility Eskom ([link](#))**
- **Argentine central bank tightens monetary policy as inflation expectations rise ([link](#))**
- **Indian government announces further capital infusions for state-owned banks ([link](#))**
- **Bank Indonesia leaves its policy rate unchanged at 6%, as expected ([link](#))**

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Global markets range-bound as investors weigh trade and policy outlooks

Risk assets are mixed with further gains being tempered by continued political overhang. In the US, the S&P 500 advanced moderately on earnings beats and stronger commodity prices that drove sector-specific gains, while Treasury yields were 1-2 bps higher across the curve following the release of the January FOMC minutes. The account of the meeting showed the committee favored ending balance sheet normalization by year end, but maintained a slight tightening bias on policy rates if inflation outcomes are higher than projected. Overnight, Asian and European bourses recovered from early losses on media reports that suggest the US and China continue to head towards a trade agreement. Relatedly, the US dollar appreciation has lost some momentum amid ongoing speculation that the US-China trade deal could include an FX provision around yuan stability. Brexit negotiations remain closely watched with the sterling appreciating on optimism about the potential for a compromise between the UK's PM May and the EU's Juncker around the Irish border. In EM, the focus was on the South African budget statement and its implications for Eskom, as well as the submission of the Brazilian pension reform details to Congress.

Key Global Financial Indicators

Last updated: 2/21/19 8:08 AM	Level		Change from Market Close				
	Last 12m	Latest	1 Day	7 Days	30 Days	12 M	YTD
Equities					%		%
S&P 500		2785	0.2	1	4	3	11
Eurostoxx 50		3262	0.1	2	4	-5	9
Nikkei 225		21464	0.2	2	4	-2	7
MSCI EM		43	0.0	1	3	-13	9
Yields and Spreads					bps		
US 10y Yield		2.67	1.1	2	-11	-28	-1
Germany 10y Yield		0.13	3.3	3	-12	-59	-11
EMBIG Sovereign Spread		352	-4	-3	-23	67	-62
FX / Commodities / Volatility					%		
EM FX vs. USD, (+) = appreciation		63.7	0.0	1	1	-10	2
Dollar index, (+) = $ appreciation		96.5	0.0	-1	0	7	0
Brent Crude Oil ($/barrel)		67.0	-0.1	4	7	2	25
VIX Index (%, change in pp)		14.3	0.3	-1	-4	-6	-11

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

United States

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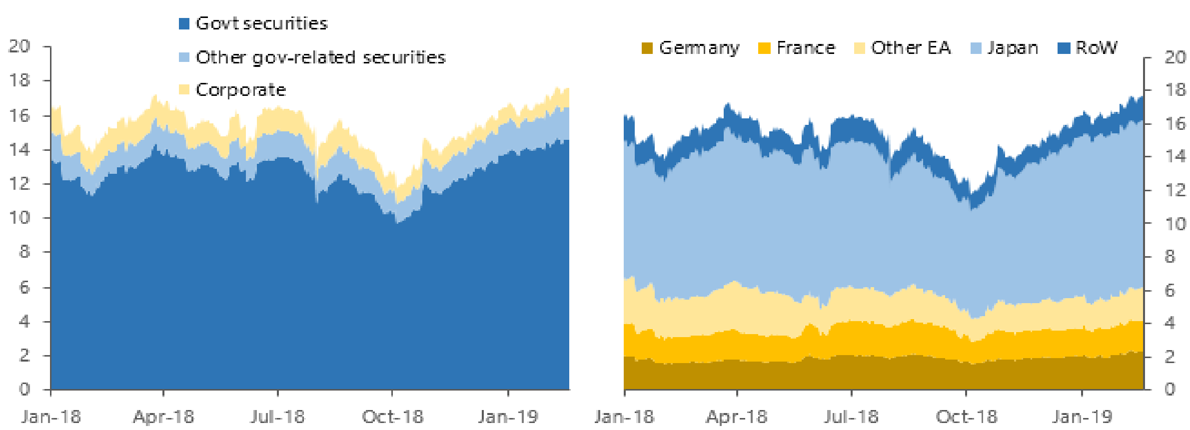
The FOMC January meeting minutes showed the committee expects to end balance sheet normalization by year end, but uncertainty remains around the interest rate path. On the balance sheet, "almost all participants" considered it "desirable to announce before too long a plan to stop" normalization "later this year". As expected, the Fed plans to reinvest mortgage maturities in Treasuries after overall balance sheet reduction is complete. **On the policy rate**, "many participants suggested that it was not yet clear what adjustments … may be appropriate later this year" given muted inflation pressure and "less stretched" asset valuations. "Several" think further rate hikes are warranted only if inflation overshoots projections. **On the shift to a "patient" policy stance**, the approach was explained as "an appropriate step in managing various risks and uncertainties in the outlook", including from low inflation, slowing global growth, the government shutdown, and the ability to evaluate the effect of rate hikes. **The effectiveness of the FOMC "dot plot" was also discussed**. "A few participants expressed concerns that in the current environment of increased uncertainty", the dot plot "does not accurately convey the Committee's policy outlook", and the "the public had misinterpreted the median or central tendency of those projections as representing the consensus view of the Committee or as suggesting that policy was on a preset course."

The minutes were perceived as less dovish than expected, partly due to the surprisingly dovish tone in the January post-meeting statement. The 2-year yield rose 3 bps after the release, up 1 bp for the day to 2.49%. Similarly, the 10-year yield rose 1 bp to 2.65%. The implied yield of the Dec-2019 Fed funds futures was unchanged at 2.37%, with the Dec-2020 yield up 2 bps to 2.14%. Breakeven rates continued to widen on the rally in energy prices. The 2- and 10-year rates each rose 2 bps to 1.67% and 1.89% respectively, both at 3-month high. Stock markets were little changed after the minutes, with major indices closing marginally higher (S&P 500 +0.2%). Amongst the key data releases this morning, durable goods orders ex-transportation was marginally up by 0.1% mom in December (vs expectations of a 0.3% increase), while the headline number also rose by less than expected at 1.2% mom (vs expectations of a 1.7% increase). US equity futures and Treasury yields were little changed following the release.

The amount of negative yielding fixed income securities has nearly doubled since October 2018 to about 20% of amounts outstanding as benchmark rates in advanced economies fell on global growth worries, trade tensions and other political risks. Of the $51 tn Barclays' Global Aggregate index, almost 20% of the member securities are carrying negative yields, up from 12% in late October, but still down from the peak of 30% back in 2016. The majority of increase is in government securities, mostly from Japan and euro area (equally split among Germany, France and other euro area countries).

Negative Yielding Fixed Income Securities
(share of Barclays Global Aggregate index by market cap)
Source: Bloomberg.



Europe

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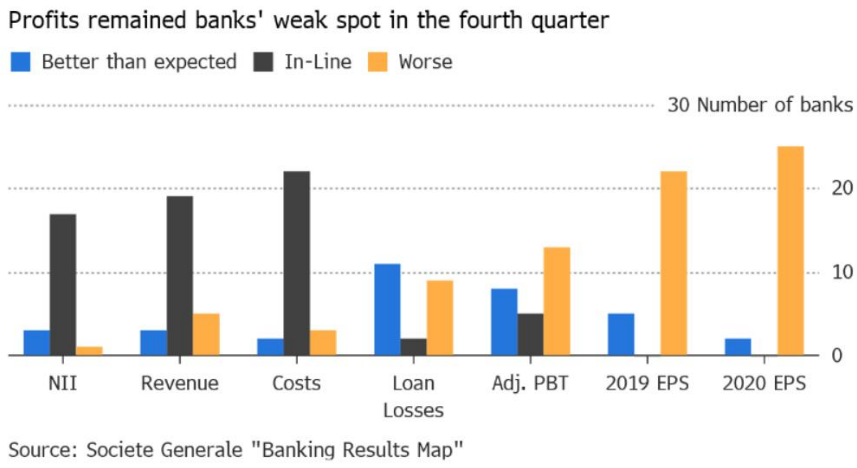
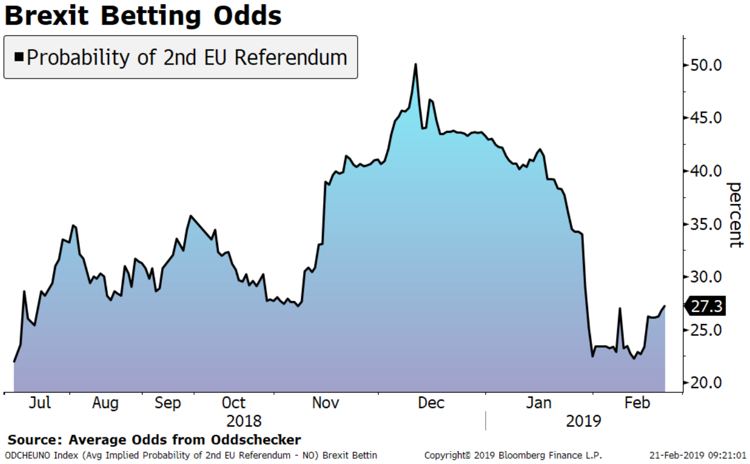
Equities and fixed income markets are mixed in the region. The EuroStoxx 600 is down slightly, with most bourses trading in narrow ranges. The UK FTSE 100 (-0.7%) is underperforming after lower earnings for some of its major constituents. The banking sector is underperforming (-0.7%) after downbeat earnings reports, even though Barclays (+3.4%) is outperforming after it beat Q4 earnings projections and expectations for buybacks. In general, European banks continue to report weak revenues, low margins, and shrinking fees. Yields are unchanged in core markets but falling 3-4 bps in Italy.



United Kingdom

PM May and EC President Juncker remain engaged in talks over a more palatable solution to the Irish backstop issue. Initial headlines have given investors some ground for optimism, but nothing concrete has been released. On the domestic front, three Conservative MPs resigned to join the new Independent group formed by former Labour MPs; the group has 11 members now. The implied probability of a second referendum (which members of the Independent group support) has ticked higher over the last few days, with betting odds rising to 27%. This is the highest level in three weeks but still well below the December peak of 50%.



Fitch Ratings placed the UK (rated AA) on negative watch citing an increased chance of a no-deal Brexit. The outlook for the credit rating will be resolved "during the first half of this year, in light of the modalities of the UK's scheduled exit from the EU."

Other Mature Markets

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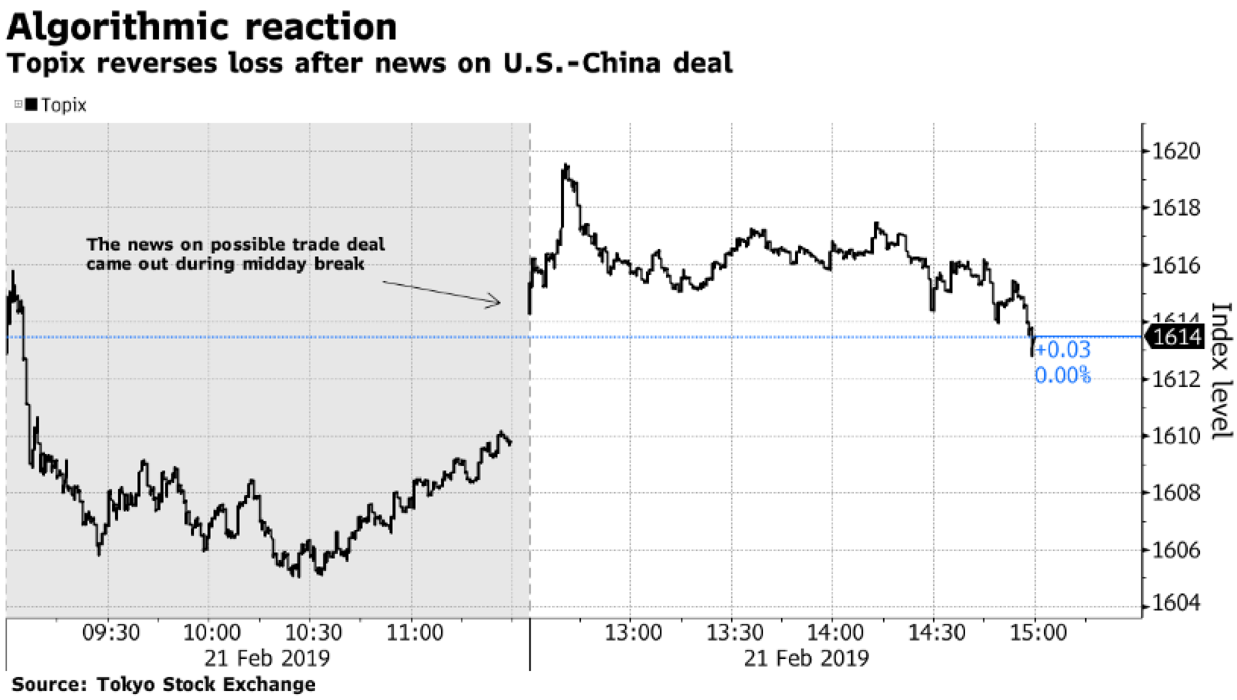
Japan

Equities (Topix 0.0%; Nikkei +0.2%) were broadly flat as investors were weighing trade optimism against disappointing Japanese economic data. Japan's manufacturing PMI fell into contractionary territory of 48.5 in February, the first time in two and half years, from 50.3 in January. This was mainly due to a fall in production and new orders. Poor manufacturing activity followed weak exports data for January that was released yesterday. Japanese exports contracted by -8.4% yoy, marking a deterioration from -3.8% yoy in December. The main drag on Japanese overseas shipments was poor exports to China, Japan's largest export partner, falling by 17% yoy. **10-year JGB yields fell 0.5bps to -0.05%. The yen appreciated 0.1%.**



Emerging Markets

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Latin American assets were mixed yesterday. In equities, Brazil (-1%) saw the largest losses as investors focus on the government's ability to approve the proposed pension reform bill, while Argentina (+0.6%), Chile (+0.5%) and Mexico (+0.5%) all saw gains. Among regional currencies, the Colombian peso (+1%) and Chilean peso (+0.6%) saw gains as commodity prices went up, while the Argentine peso (-1%) weakened for the 13th consecutive day as traders continue to adjust their position to high inflation expectations. **Asian equities gained** (+0.3%) helped by news reports on progress in US-China trade negotiations. According to Reuters, the US and China have started to outline commitments in principle on the stickiest issues in their trade dispute, marking the most significant progress yet. Regional currencies were broadly stable against the dollar. In **EMEA, equity markets are mixed but trading in narrow ranges**. The most notable move in currencies has been the South African rand, appreciating 0.7% in the wake of positive budget announcements.

Key Emerging Market Financial Indicators

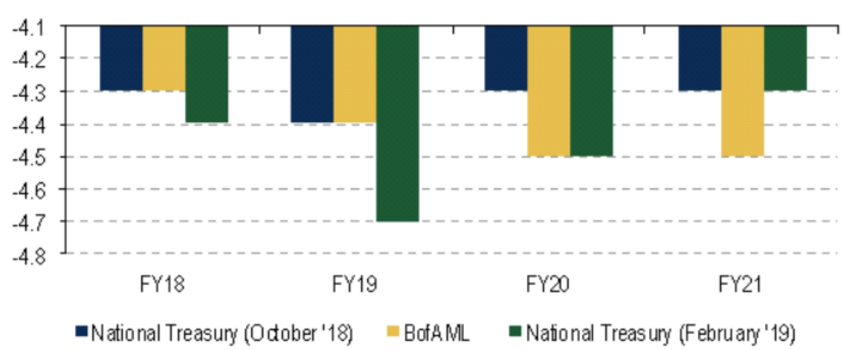
Last updated:	Level		Change				
2/21/19 8:13 AM	Last 12m	index	1 Day	7 Days	30 Days	12 M	YTD
Major EM Benchmarks					%		%
MSCI EM Equities		42.66	0.0	1	3	-13	9
MSCI Frontier Equities		28.60	-0.5	-1	3	-18	9
EMBIG Sovereign Spread (in bps)		351	-5	-4	-24	66	-63
EM FX vs. USD		63.66	-0.1	1	1	-10	2
Major EM FX vs. USD			%, (+) = EM currency appreciation				
China Renminbi		6.72	0.0	1	1	-6	2
Indonesian Rupiah		14071	-0.2	0	1	-3	2
Indian Rupee		71.25	-0.2	0	0	-9	-2
Argentine Peso		39.65	0.0	-4	-5	-50	-5
Brazil Real		3.74	-0.3	-1	0	-13	4
Mexican Peso		19.22	0.0	0	0	-2	2
Russian Ruble		65.51	0.2	2	1	-13	6
South African Rand		13.96	0.4	1	-1	-16	3
Turkish Lira		5.32	0.0	-1	0	-29	-1
EM FX volatility		8.86	0.0	0.0	-0.3	0.4	-0.9

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

South Africa

The government plans to spend nearly $5 bn to bailout the country's ailing energy company Eskom. The funds will be injected over three years to help stabilize its $30 bn in debt and attempt to avoid a worsening of South Africa's energy crisis. Analysts saw the announcement as a step in the right direction. BAML noted that the effort will mean a 0.3% of GDP deterioration in the budget, but it remains broadly in line with what they had expected. The rand appreciated about 1% over the last two sessions, while its sovereign debt spreads and CDS narrowed a few basis points after the announcement.

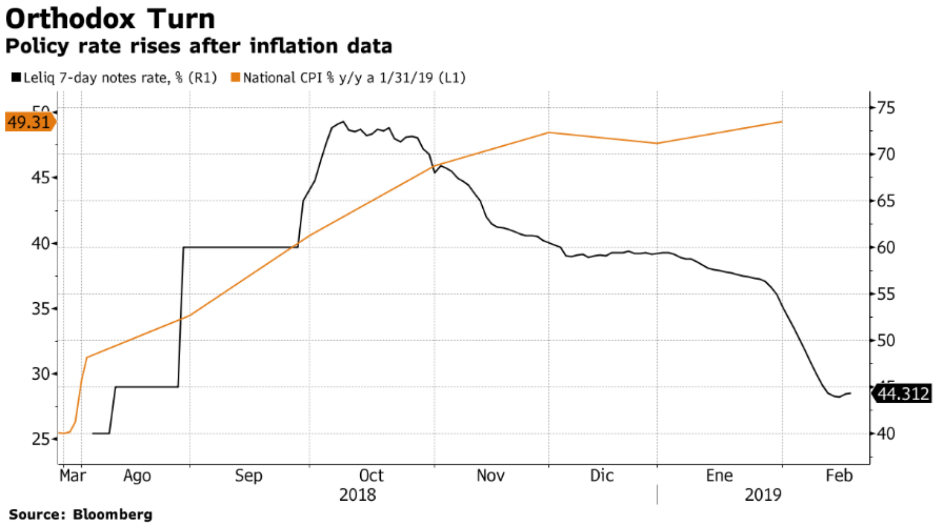
Chart of the Day: Eskom spending adds to deficit but still within our MT framework



Main budget deficit; Source: BofA Merrill Lynch Global Research, National Treasury of South Africa

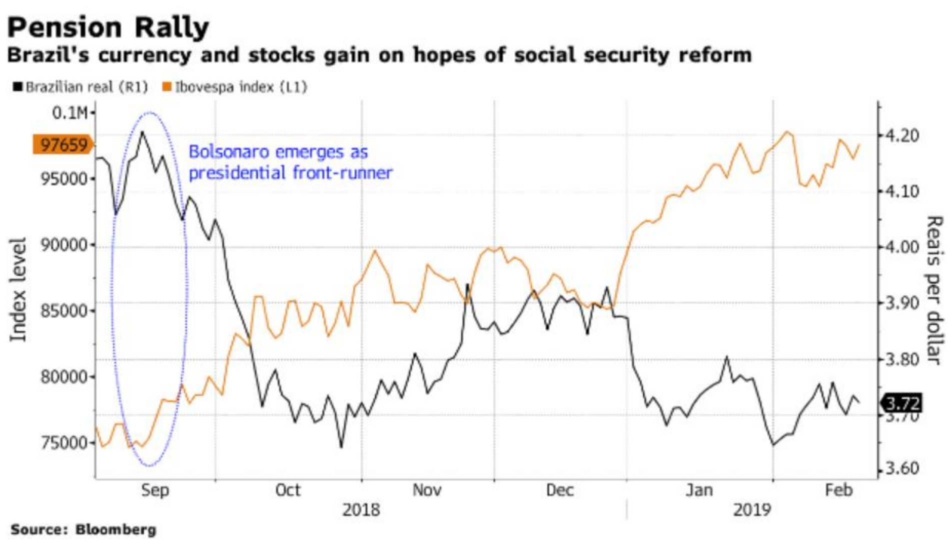
Argentina

The central bank raised its key policy rate to 46% amid private forecasts that estimate monthly inflation of as much as 3.5% in February and above 2% monthly until May. The central bank expects to surpass its monetary base goal for February by about 3%, according to a release published Monday, marking a greater monetary adjustment than the one agreed with the IMF, reports Bloomberg. This decision is in line with a second consecutive rise in its key rate, after the 2.9% inflation in January surprised the market and interrupted 3 consecutive months of disinflation. The peso (-1%) weakened against the US dollar for the 13th consecutive day as traders continued to adjust their positions to the evolving inflation expectations.



Brazil

The Brazilian government submitted the pension reform bill to Congress; however, benchmark equities fell 1.1% as investors focused on the uncertainty around the government's ability to negotiate the passage of the proposed reforms. According to analysts, the expected savings from the proposal of 1.2 trillion real ($311 bn) over 10 years are significant, and the proposal sets a minimum retirement age for both public and private sector workers of 65 for men and 62 for women, to be phased in over 12 years. Market participants expect the real to face volatility in the next few months depending on how much the bill gets delayed or watered down. Nonetheless, **the real has strengthened by 10% against dollar and the benchmark index has jumped over 30% since last September** on hopes of the pension reform's approval.

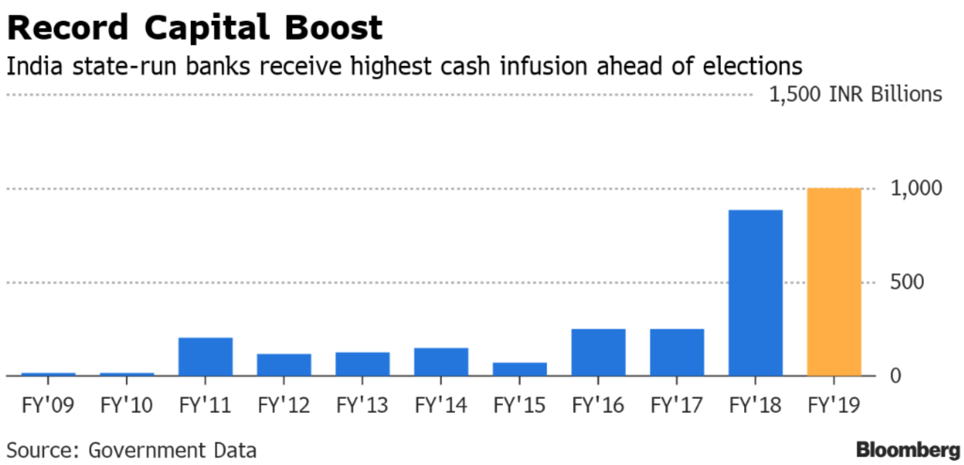


China

The PBOC's recently introduced facility to swap bank perpetual bills was used for the first time. The PBOC swapped RMB1.5 bn ($223 mn) worth of 1-year central bank bills for perpetual bonds with a coupon of 2.45%. **The facility, set up on January 24, aims to enhance the attractiveness of banks' perpetual bonds which count toward additional Tier 1 capital**. So far, Bank of China has issued RMB40 bn worth of perpetual bonds. Chinese equities underperformed regional markets (-0.3%), despite further positive news flow on a US-China trade deal.

India

Share prices of state-owned banks rallied as the government announced additional capital injections. As part of the government's recapitalization program, India announced that it will inject INR482 bn ($6.8 bn) into 12 state-controlled lenders. This would bring the total infusion for the year ending March 31 to INR1 tn. The government had in October 2017 said it would pump a total of INR2.11 tn into state-run lenders over two years. Indian banks have been plagued by elevated levels of bad debt, and the recapitalization is aimed at boosting lending. In turn, banks are required to implement reforms and address asset quality issues. **The benchmark stock index posted modest gains on the day (+0.3%).**



Indonesia

Bank Indonesia (BI) left its 7-day reverse repo rate unchanged at 6%, as expected. The decision was the third straight month that the central bank left interest rates unchanged, after hiking by six times for a total of 175 bps in 2018. The statement mentioned that BI remains focused on maintaining external stability by maintaining the attractiveness of domestic financial assets and to control the current account deficit. At the same time, BI also noted that it would be looking to introduce macroprudential policies in an effort to support economic activity. **The Indonesian rupiah depreciated 0.3% while equities rose 0.4% today.**

Ecuador

The IMF and Ecuador reached a staff-level agreement on a $4.2 bn extended fund facility. The arrangement is part of a broader effort of the international community that includes financial support of almost $6 bn over the next three years from the Development Bank of Latin America, the Inter-American Development Bank, the Latin American Reserve Fund, and the World Bank. Yields on 10-year bonds fell from 10.1% to 9.7% following the announcement.

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Global Financial Indicators

Last updated: 2/21/19 8:08 AM	Level		Change				
	Last 12m	Latest	1 Day	7 Days	30 Days	12 M	YTD
Equities					%		%
United States		2785	0.2	1	4	3	11
Europe		3262	0.1	2	4	-5	9
Japan		21464	0.2	2	4	-2	7
China		2752	-0.3	1	5	-14	10
Asia Ex Japan		69	0.8	1	4	-11	9
Emerging Markets		43	0.0	1	3	-13	9
Interest Rates					basis points		
US 10y Yield		2.67	1.1	2	-11	-28	-1
Germany 10y Yield		0.13	3.3	3	-12	-59	-11
Japan 10y Yield		-0.04	-0.5	-2	-5	-9	-4
UK 10y Yield		1.22	3.8	7	-10	-34	-6
Credit Spreads					basis points		
US Investment Grade		122	0.5	2	-10	33	-25
US High Yield		420	-4.5	-2	-10	75	-101
Europe IG		66	0.7	-5	-9	14	-21
Europe HY		293	2.6	-16	-25	27	-60
EMBIG Sovereign Spread		352	-4.0	-3	-23	67	-62
Exchange Rates					%		
Dollar Index (DXY)		96.48	0.0	-1	0	7	0
USDEUR		1.14	0.1	1	0	-8	-1
USDJPY		110.7	0.1	0	-1	-3	-1
EM FX vs. USD		63.7	0.0	1	1	-10	2
Commodities					%		
Brent Crude Oil ($/barrel)		67	-0.1	4	7	2	25
Industrials Metals (index)		119	-0.5	3	5	-14	9
Agriculture (index)		42	0.9	-1	-2	-14	2
Implied Volatility					%		
VIX Index (%, change in pp)		14.3	0.3	-1.4	-3.5	-5.7	-11.1
10y Treasury Volatility Index		3.5	-0.2	-0.3	-0.4	-1.4	-1.1
Global FX Volatility		7.8	0.0	-0.1	-0.3	-0.6	-1.2
EA Sovereign Spreads					10-Year spread vs. Germany (bps)		
Greece		364	-4.3	-12	-27	-8	-52
Italy		271	-5.1	1	20	138	21
Portugal		138	-4.0	-9	-12	10	-10
Spain		107	-2.8	-7	-4	28	-10

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: 2/21/2019 8:13 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		6.72	0.0	0.8	1	-6	2		3.1	-0.2	2	1	-88	-13
Indonesia		14071	-0.2	0.1	1	-3	2		8.0	-8.2	-1	-29	124	-17
India		71	-0.2	-0.1	0	-9	-2		7.5	-1.9	4	-9	-33	5
Philippines		52	-0.1	0.5	1	0	1		5.6	-0.5	-5	-23	85	-67
Thailand		31	-0.4	0.5	2	1	4		2.6	-0.2	2	-5	23	-2
Malaysia		4.08	-0.2	-0.1	1	-4	1		4.0	-0.5	3	-6	-6	-12
Argentina		40	0.0	-3.6	-5	-50	-5		20.6	59.0	38	-61	486	-241
Brazil		3.74	-0.3	-0.6	0	-13	4		7.8	8.7	0	-24	-83	-35
Chile		654	-0.2	2.0	3	-9	6		4.3	-1.1	-2	-17	-50	-13
Colombia		3112	0.0	1.3	0	-7	4		6.4	1.1	-4	-15	-1	-11
Mexico		19.22	0.0	0.2	0	-2	2		8.4	1.1	-17	-29	64	-31
Peru		3.3	-0.1	0.6	0	-2	2		5.6	0.6	-2	-10	66	-12
Uruguay		33	0.0	-0.3	0	-13	-1		10.2	-0.3	1	-3		-47
Hungary		279	0.1	0.9	0	-9	0		2.0	-5.6	-6	-16	33	-22
Poland		3.82	0.0	0.4	-1	-11	-2		2.2	-2.6	-5	-12	-57	-10
Romania		4.2	0.0	0.1	-1	-9	-3		4.2	7.0	1	-25	14	-8
Russia		65.5	0.2	1.7	1	-13	6		8.1	0.3	9	7	127	-28
South Africa		14.0	0.4	1.2	-1	-16	3		9.5	-10.3	-15	-8	77	-7
Turkey		5.32	0.0	-1.0	0	-29	-1		15.7	20.1	38	-93	370	-122
US (DXY; 5y UST)		96	0.0	-0.6	0	7	0		2.50	2.9	2	-13	-19	-1

	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		2752	-0.3	1	5	-14	10		179	-3	-6	-4	17	-15
Indonesia		6538	0.4	2	1	-2	6		198	-1	0	-5	37	-38
India		35898	0.4	0	-2	6	0		164	-3	-5	-21	49	-32
Philippines		7931	-0.1	-1	-1	-8	6		91	-1	-3	-6	-1	-30
Malaysia		1731	0	2	2	-7	2		124	-1	-4	-22	12	-38
Argentina		36504	0.6	-1	3	10	21		709	-3	31	36	307	-106
Brazil		96545	-1.1	-2	1	12	10		236	-2	-2	-7	9	-37
Chile		5414	0.1	1	-1	-5	6		134	-2	-6	-10	15	-32
Colombia		1479	0.1	0	6	-3	12		191	-2	-7	-3	15	-37
Mexico		43178	0.5	2	-2	-11	4		321	-1	2	9	85	-33
Peru		20627	1	2	5	0	7		142	-2	-3	-6	8	-26
Hungary		40522	-0.1	2	-1	4	4		113	-2	-3	-21	12	-35
Poland		60412	0.0	2	1	-3	5		52	-3	-4	-10	-13	-33
Romania		7812	0.8	2	9	-6	6		199	2	6	-14	74	-22
Russia		2477	-0.4	1	0	7	5		221	-5	-2	4	66	-31
South Africa		55687	0.0	2	3	-5	6		298	-7	-11	-27	73	-67
Turkey		102601	0.6	0	5	-12	12		414	1	8	-11	126	-15
Ukraine		555	0.2	-2	0	65	-1		685	-14	-47	0	267	-102
EM total		43	0.0	1	3	-13	9		351	-5	-4	-24	66	-63

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