GLOBAL MARKETS ANALYSIS
Monetary and Capital Markets

Global Markets Monitor

THURSDAY, FEBRUARY 23, 2023

- **US GDP weaker than expected** (link)
- **Markets narrow gap with Fed dots** (link)
- **Congressional Budget Office predicts US budget deficit to exceed $1.5 trillion** (link)
- **China to use fiscal policy to boost economy** (link)
- **Oil prices still under pressure** (link)
- **Bank of Korea is latest central bank to turn hawkish** (link)
- **Türkiye cuts less than expected** (link)

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Markets cautiously optimistic as expectations align

Risk sentiment was positive this morning as market expectations for future Fed interest rate policy moved closer to the Fed's dot plot projections. Many analysts were worried that earlier market forecasts were too dovish, raising the risk of market volatility and a potential selloff. A number of positive corporate earnings reports also boosted sentiment. The minutes from the latest FOMC meeting on February 1 contained few surprises and had a negligible impact on markets, with contacts pointing out that the significance of the meeting was limited because it predated key data releases on employment and inflation. The Bank of Korea was the latest central bank to turn hawkish, joining the ranks of the Fed, the ECB, the RBA, the Riksbank, the Norges Bank, the Mexican central bank, and the Polish central bank among many others as inflation continues to bedevil policymakers. Markets in South Africa reacted positively to news that the government would introduce a debt relief package for Eskom, the troubled state utility company.

Key Global Financial Indicators

Last updated: 2/23/23 8:03 AM	Level		Change from Market Close					Since
	Last 12m	Latest	1 Day	7 Days	30 Days	12 M	YTD	23-Feb-22
Equities					%		%	
S&P 500		3991	-0.2	-4	-1	-6	4	-6
Eurostoxx 50		4267	0.6	-1	3	7	12	7
Nikkei 225		27104	-1.3	-1	1	2	4	2
MSCI EM		39	-0.5	-4	-7	-18	3	-18
Yields and Spreads					bps			
US 10y Yield		3.95	3.3	9	44	196	7	196
Germany 10y Yield		2.55	2.6	7	34	232	-3	232
EMBIG Sovereign Spread		456	3	11	14	54	5	44
FX / Commodities / Volatility					%			
EM FX vs. USD, (+) = appreciation		50.5	0.0	0	-1	-5	1	-5
Dollar index, (+) = $ appreciation		104.5	-0.1	1	2	9	1	9
Brent Crude Oil ($/barrel)		81.6	1.2	-4	-8	-16	-5	-16
VIX Index (%, change in pp)		21.9	-0.4	4	2	-9	0	-9

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

Mature Markets

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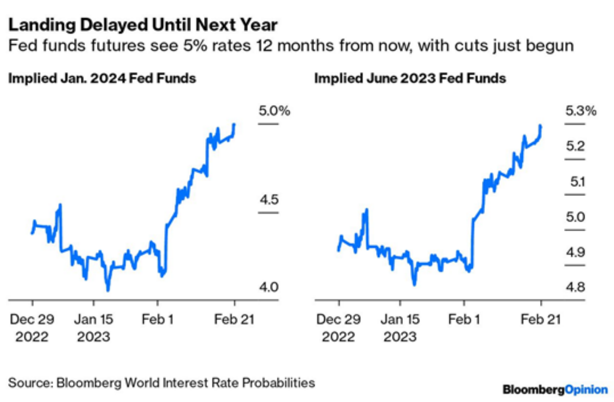
United States

The latest US Q4 GDP estimate came in weaker than forecasts, while inflation data were higher than expected. Treasuries sold off on the news, while the dollar appreciated against the euro. US equity index futures gave back some of their early gains. Tomorrow's PCE inflation data report will now take on even more significance.

Selected US Economic Data 8.30am EST
Source: Bloomberg

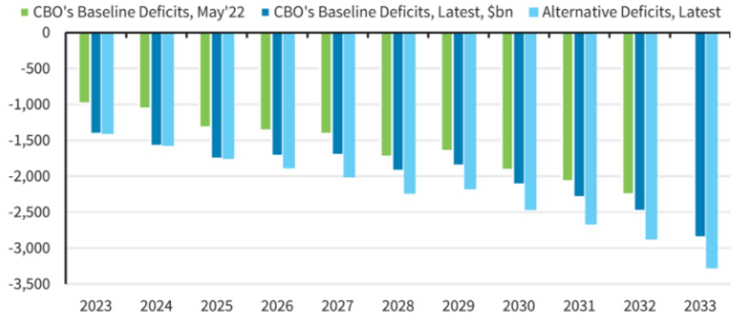
Data Point	Consensus Forecast	Actual Outcome
Q4 GDP Annualized	**2.9% (quarter on quarter)**	**2.7%**
Personal Consumption	**2%**	**1.4%**
Q GDP Price Index	**3.5%**	**3.9%**
Q4 Core PCE	**3.9% (quarter on quarter)**	**4.3%**

Markets are narrowing the gap with the Fed dot plot as investors acknowledge that Fed policy will need to remain tight for longer than originally expected. At the start of the year, markets expected the Fed Funds policy rate to peak below 5% in the first half of 2023 and predicted three rate cuts by the end of the year, a very dovish path compared to the Fed dot plot. However, the recent selloff in the Treasury markets has led to a repricing of the future path of Fed policy. With interest rates close to their highest levels of the year, the Fed Funds futures market now expect a peak policy rate of just under 5.35%, with just one rate cut over the next 12 months. Higher interest rate volatility and higher interest rates could revise these expectations in an even more hawkish direction.



The Congressional Budget Office (CBO) now predicts that the US budget deficit will exceed $1.5 tn every year starting in 2024. The CBO also expects the cumulative deficit to exceed $3 tn over the next decade. If certain provisions in the 2017 tax package are extended, the deficits will be even higher. The debt to GDP ratio is projected to increase from 97% at the end of Fiscal Year (FY) 2022 to 100% by the end of FY 2024 and 118% by the end of FY 2033. Market forecasts for deficits are much more benign, with the consensus forecast at 4.4% of GDP over FY 2023–25 versus 5.8% for the CBO. Larger deficits will result in higher issuance of Treasuries, which could in turn lead to higher interest rates. Markets may be overly complacent about these potential risks.

Figure 1. CBO expects budget deficits to be north of $1.5trn every year from 2024 onward



Alternative scenario assumes extension of 2017 individual income tax provisions

Source: CBO, Barclays Research

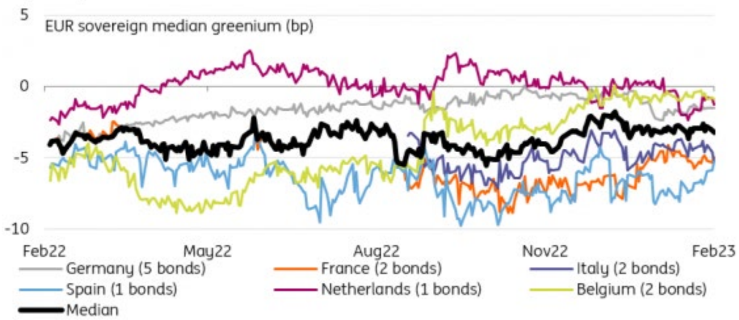
Euro area

Equities (+0.4%) edged higher after the FOMC minutes were not as hawkish as some had feared. The focus of contacts is also on geopolitics as they await further details on China's position and new sanctions on Russia, including steps to avoid the circumvention of existing sanctions. The EU is expected to announce a 10th package of sanctions as tomorrow marks one year since the start of the war.

Final data showed euro area core inflation at 5.3% yoy in January compared to 5.2% expected, which contributed to a rise of 2–3 bps in euro area rates. There is a broad consensus that the ECB will hike 50 bps in March but markets price a 40% chance of a further 50 bps hike in May. Contacts are also divided on the likelihood of a hike of 50 bps versus 25 bps in May.

Analysts at ING argue that the greenium on euro area bonds has fallen as supply caught up with demand. The median greenium on the large European government bond issuers went from around 4 bps in 2022 to 3 bps in 2023. Another factor may be that a higher rate environment with ample primary supply is requiring a larger concession to buyers. The greenium refers to the observation that yields on "green" sovereign bonds trade below yields on equivalent "brown" sovereign bonds.

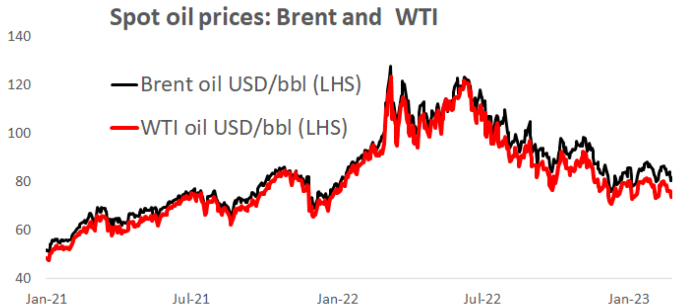
The euro sovereign greenium cheapened last year as market liquidity worsened



Source: Refinitiv, ING

Commodity prices

Brent oil prices have traded 5% lower in the past five days despite better-than-expected economic data in several countries and news of China's reopening. Analysts commented that pricing on physical markets may indicate slack in the global system. Oil prices (+1%) are higher today following an unexpectedly sharp drop of almost 3% yesterday.



Note: Bloomberg and IMF

Emerging Markets

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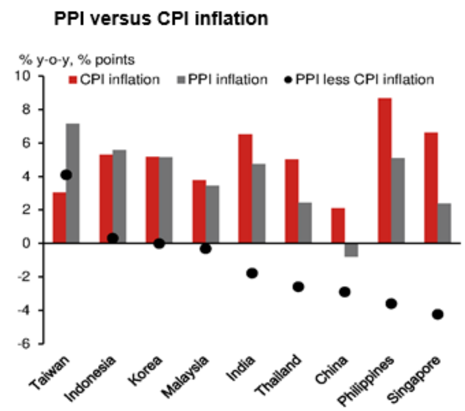
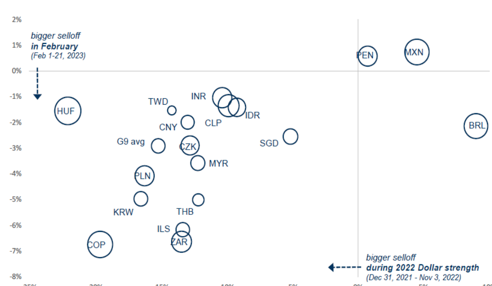
EMEA equities were mostly trading higher while currencies were little changed against the dollar. On the data front Hungary's average gross wages surprised on the upside in December (+18.1%y/y versus expected 17.0% from 16.8%). In Poland, the unemployment rate increased to 5.5% in January, in line with expectations (from 5.2%). **Stocks in Asia were mixed, with strong gains in Taiwan POC and losses in Singapore.** Local currencies appreciated. Regional inflation may be close to an inflection point, according to Nomura. The gap between PPI and CPI inflation, a rough proxy of margins, currently suggests firms are using lower costs to recoup their lost profit margins after last year's squeeze, rather than pass on the benefit to consumers. **Equity markets in Latin America lost ground,** although several local currencies appreciated due to the weak dollar. Brazil announced the reinstitution of federal taxes on ethanol and gasoline, which analysts fear could put upward pressure on inflation which still remains higher than the central bank target (5.77% versus the 4.75% upper bound).



Emerging Market (EM) Currencies

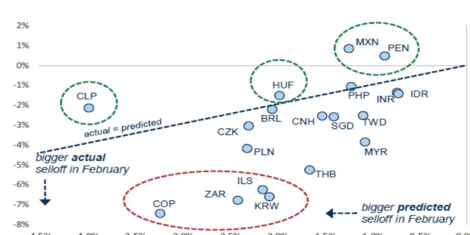
EM currencies display varying sensitivities to the dollar. Some are more resilient even if the dollar appreciates strongly, while others such as the South African rand, the Colombian peso and the Korean won are more vulnerable to a stronger dollar and higher US yields. The Mexican peso is among the strong performers due to the country's close ties with the still booming US economy. Improving economic activity in China and Europe has led to the strength in currencies such as the Hungarian Forint and Chilean peso in the current episode.

Exhibit 1: February price action is reminiscent of Dollar strength in 2022
% spot appreciation of the displayed currency vs USD between the displayed dates. Bubble sizes reflect current levels of 12m nominal carry.



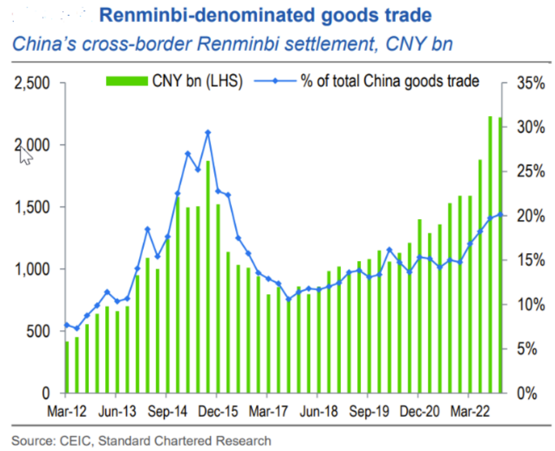
Source: Bloomberg, Goldman Sachs Global Investment Research

Exhibit 2: In addition to MXN, HUF and CLP have outperformed in February, potentially reflecting improving growth expectations in Europe and China
Actual (y-axis) vs predicted (x-axis) appreciation vs USD from Feb 1 to Feb 21. Predictions reflect recent sensitivities to G9 FX, and key global market factors, including US yields.



Source: Thomson Reuters, Goldman Sachs Global Investment Research

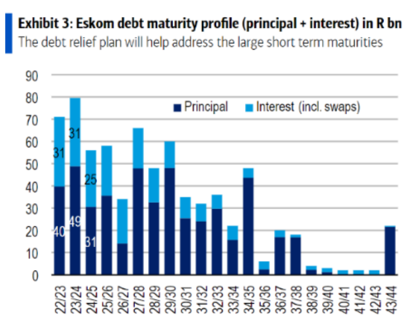
China

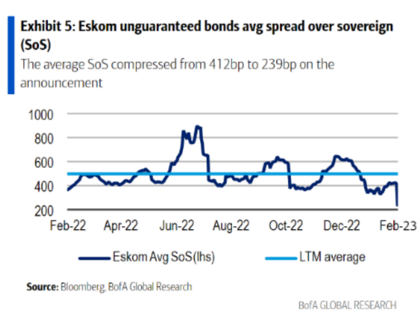


Fiscal policy will place more efforts in 2023 on anchoring market expectations, stabilizing investment and boosting consumption, according to a speech by Finance Minister Liu Kun. He noted that fiscal policy tools should support both rigid demand for housing and housing improvement and boost the stable development of the real estate market. The policy mix of fiscal deficit and discount on special local government bonds will be optimized, and the intensity of fiscal expenditure will be properly increased. Separately, **Renminbi's share as a trade settlement currency has continued to improve in Q4 2022, according** to Standard Chartered. Renminbi-settled goods trade stayed high as a share of total China goods trade, at 20% in Q4 2022 gaining from H1's juts below 18% on average in January-June 2022. **Equities declined marginally** (**Shanghai -0.1%, Shenzhen -0.2%). Chinese renminbi and 10Y bond yields were little changed**. The People's Bank of China (PBOC) reversed a five-day net injection to drain cash from the banking system as money market tension eased while repo rates fell. Separately, **PBOC issued guidelines encouraging companies and financial organizations in Guangdong and Hengqin to sell yuan bonds and foreign currency bonds in Macau**.

South Africa

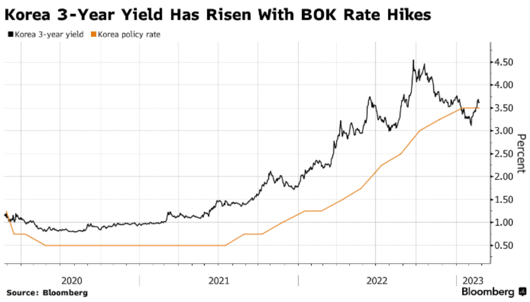
Markets reacted positively to the budget announcements which showed improved fiscal deficit projections, with the fiscal deficit expected to narrow to 4.2% of GDP in the current year. In the aftermath of the budget announcement the rand reversed earlier losses against the dollar while 10y yields eased (-8bps). Investors were closely watching announcements related to power utility Eskom's debt. In this regard the finance minister announced that the government would give Eskom R254bn ($13.9bn) of debt relief over the next 3 years: R168bn would be allocated to principal repayments and the balance allocated towards interest payments. R184bn of the R254 support is coming from an interest-free subordinated shareholder loan that is set to be converted to equity on a quarterly basis subject to certain operational conditions. Analysts' commentary was mostly positive, with Deutsche Bank highlighting that the size of the debt support for Eskom was a positive surprise.





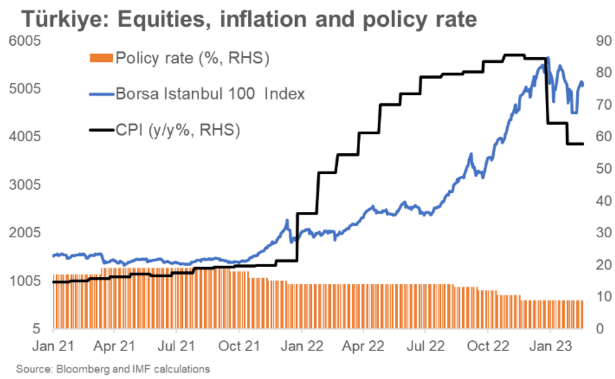
South Korea

The Bank of Korea (BOK) became the latest entrant to the club of hawkish central banks. It kept its policy rate unchanged at 3.5% as expected but signaled a continued hawkish stance. The BOK statement noted that Korean inflation is likely to fall at a slower pace than other major economies, given the potential for a rise in utility costs. The economic growth forecast for 2023 was revised down to 1.6% from 1.7% and the inflation forecast to 3.5% from 3.6%. Governor Changyong said the BOK is keeping the door open for further policy tightening to counter inflation. During the press conference, he also mentioned that five of the six board members he polled were open to borrowing costs reaching a peak of 3.75% after holding the seven-day repurchase rate at 3.5%. **Equities gained (+0.9%), 10Y yields declined -4.6 bps, the won strengthened +0.6%.**



Türkiye

The Central Bank of the Republic of Türkiye (CBRT) cut its policy rate by 50 bps to 8.5%, while consensus had expected a 100bps cut. The press statement noted that while the earthquake is expected to negatively impact short-term economic activity, the medium-term impact will be more limited. As regards inflation, the statement noted that the underlying trend had improved. The statement highlighted the importance of keeping financial conditions supportive. Turkish equities were trading higher this morning (+0.7%) while the lira was little changed.



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Global Financial Indicators

2/23/23 8:03 AM	Level		Change				YTD	Since
	Last 12m	Latest	1 Day	7 Days	30 Days	12 M		23-Feb-22
Equities					%		%	%
United States		4005	-0.2	-3	0	-5	4	-5
Europe		4267	0.6	-1	3	7	12	7
Japan		27104	-1.3	-1	1	2	4	2
China		4104	-0.1	0	-2	-9	6	-11
Asia Ex Japan		67	-0.6	-4	-8	-15	3	-16
Emerging Markets		39	-0.5	-4	-7	-18	3	-18
Interest Rates					basis points			
US 10y Yield		3.95	3.3	9	44	196	7	196
Germany 10y Yield		2.55	2.6	7	34	232	-3	232
Japan 10y Yield		0.51	0.0	0	12	31	8	31
UK 10y Yield		3.65	5.4	16	29	218	-2	218
Credit Spreads					basis points			
US Investment Grade		146	0.6	5	-2	5	-13	3
US High Yield		459	-1.8	11	13	53	-21	53
Europe IG		79	-1.8	3	0	8	-11	8
Europe HY		410	-9.5	17	-6	59	-64	59
Exchange Rates					%			
USD/Majors		104.46	-0.1	1	2	9	1	9
EUR/USD		1.06	0.1	-1	-2	-6	-1	-6
USD/JPY		135.0	0.1	1	3	17	3	17
EM/USD		50.5	0.0	0	-1	-5	1	-5
Commodities					%			
Brent Crude Oil ($/barrel)		81.6	1.2	-4	-7	-3	-5	-5
Industrials Metals (index)		164	-0.9	1	-7	-13	-1	-13
Agriculture (index)		70	-0.1	1	5	0	2	0
Implied Volatility					%			
VIX Index (%, change in pp)		21.9	-0.4	3.6	2.1	-9.2	0.2	-9.2
US 10y Swaption Volatility		119.8	2.6	9.1	1.8	25.5	-5.9	25.5
Global FX Volatility		10.2	0.0	0.0	0.0	2.8	-0.5	2.8
EA Sovereign Spreads					10-Year spread vs. Germany (bps)			
Greece		189	-2.1	9	-12	-51	-16	-51
Italy		191	-2.6	6	9	20	-23	20
Portugal		88	-2.0	0	0	-4	-14	-4
Spain		97	-1.9	0	0	-7	-13	-7

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

Emerging Market Financial Indicators

Last updated: 2/23/2023 8:06 AM	Exchange Rates								Local Currency Bond Yields (GBI EM)							
	Level		Change (in %)					Since	Level		Change (in basis points)					Since
	Last 12m	Latest	1 Day	7 Days	30 Days	12 M	YTD	23-Feb-22	Last 12m	Latest	1 Day	7 Days	30 Days	12 M	YTD	23-Feb-22
		vs. USD	(+) = EM appreciation							% p.a.						
China		6.90	-0.1	-0.6	-2	-8	0	-8		3.2	2.0	8	3	39	19	39
Indonesia		15192	0.1	-0.2	-1	-6	3	-6		6.8	2.0	10	16	29	-15	29
India		83	0.1	0.0	-2	-10	0	-10		7.7	-0.1	22	23	96.1	21	
Philippines		55	0.5	0.4	-1	-7	2	-7		6.0	0.0	5	0	98	-5	98
Thailand		35	-0.3	-1.1	-6	-7	0	-7		2.7	0.5	1	23	50	9	50
Malaysia		4.43	0.2	-0.7	-3	-6	-1	-6		3.9	-0.2	2	17	24	-14	24
Argentina		195	0.0	-1.1	-5	-45	-9	-45		87.3	-57.0	14	225	3960	-93	3932
Brazil		5.15	0.1	1.3	1	-3	3	-3		13.5	8.9	-7	22	196	90	196
Chile		797	0.2	-0.6	2	-1	7	-1		5.6	2.0	5	38	-37	21	-37
Colombia		4898	0.0	0.6	-7	-20	-1	-20		9.8	0.0	30	-5	196	6	196
Mexico		18.32	0.2	1.1	3	10	6	10		9.1	-6.0	32	80	124	34	123
Peru		3.8	0.5	1.5	2	-2	0	-2		7.9	-0.8	-10	-3	193	-3	193
Uruguay		39	-0.5	0.8	0	8	2	8		9.9	9.8	19	-51	174	-79	174
Hungary		359	0.1	0.0	1	-11	4	-11		8.6	15.0	-2	78	375	-104	375
Poland		4.47	0.2	-0.1	-3	-9	-2	-9		6.1	9.8	44	80	215	-9	216
Romania		4.6	0.1	-0.9	-2	-6	0	-6		7.4	-6.9	8	19	229	-25	228
Russia		75.3	0.1	-0.6	-8	8	-1	8		10.6	-3.0	9	-74	-63	-131	-63
South Africa		18.3	-0.3	-0.7	-6	-17	-7	-17		9.3	8.0	24	54	175	18	175
Turkey		18.87	-0.1	-0.1	0	-27	-1	-27		10.5	-9.0	-46	36	-1193	66	-1193
US (DXY; 5y UST)		104	-0.1	0.5	2	9	1	9		4.15	-0.1	8	53	225	15	225

	Equity Markets								Bond Spreads on USD Debt (EMBIG)						
	Level		Change (in %)					Since	Level		Change (in basis points)				Since
	Last 12m	Latest	1 Day	7 Days	30 Days	12 M	YTD	23-Feb-22	Last 12m	Latest	7 Days	30 Days	12 M	YTD	23-Feb-22
										basis points					
China		4104	-0.1	0	-2	-9	6	-11		167	-4	-19	-41	-10	-41
Indonesia		6839	0.4	-1	0	0	0	-1		154	10	3	-35	14	-31
India		59606	-0.2	-3	-2	9	-2	4		150	3	3	-8	8	-4
Philippines		6686	-0.2	-2	-5	-7	2	-9		127	5	9	-13	30	-10
Thailand		1652	-0.4	0	-2	-1	-1	-3		0	0	0	0	0	0
Malaysia		1458	-0.4	-2	-3	-7	-3	-8		101	2	-6	-34	1	-32
Argentina		244719	-1.7	-5	-2	168	21	168		2099	81	215	376	-106	362
Brazil		107152	-1.9	-1	-4	-4	-2	-4		265	2	-6	-66	-9	-66
Chile		5273	-0.1	-3	-1	21	0	21		136	0	-3	-37	4	-38
Colombia		1188	-0.9	-3	-11	-21	-8	-21		421	28	57	36	49	29
Mexico		53181	-0.1	0	-2	4	10	4		367	2	14	-1	-14	-3
Peru		21705	-0.7	-1	-6	-7	2	-7		184	1	-10	-5	4	-6
Hungary		45448	0.9	-1	-3	-5	4	-5		219	11	-14	62	-3	66
Poland		59327	1.1	-2	-4	-6	3	-6		78	9	-23	66	5	62
Romania		12312	0.2	0	1	-7	6	-7		253	16	-11	30	-3	21
Russia		2212	0.0	2	1	-28	3	-28		3411	-577	938	3228	3234	2897
South Africa		78860	0.9	-2	-2	5	8	5		380	12	9	-12	13	-9
Turkey		5065	-0.1	1	-6	151	-8	151		521	4	7	-34	81	-42
Ukraine		507	0.0	0	0	-2	-2	-2		4652	210	495	3495	573	3179
EM total		39	1.1	-4	-7	-18	3	-18		393	10	26	-46	18	-65

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

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