Global Markets Monitor

Monetary and Capital Markets Department
Global Markets Analysis Division

Thursday, February 7, 2019

- **European Commission slashes growth forecast for major economies (link)**
- **ECB's 2019 bank stress test will focus on liquidity risk (link)**
- **GSIB business model shifts are congruent with the capital surcharge framework (link)**
- **Recent stock losses pressuring US public pension funds in the US (link)**
- **The Reserve Bank of India surprises with a 25 bps rate cut (link)**
- **Brazil keeps rates unchanged with no easing bias (link)**

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

Markets decline on growth worries

European equities and US futures are falling this morning as concerns about global growth are becoming more prominent. Wednesday saw the first decline in US equities in a week, and that seems set to continue today. .The European Commission cut growth forecasts for several major economies, helping to send European stocks and sovereign bond yields lower. Brexit uncertainty also continues to linger as UK PM May heads to Brussels to try to negotiate a revised deal. A number of emerging market central banks are due to announce rate decisions today. In India, the RBI surprised markets with a 25 bps cut while signaling a dovish stance. In the Philippines, the BSP kept its rate on hold as expected. Markets expect Mexico's Banxico to also keep rates steady in its announcement later today. Despite a relatively stable trading session in Asia overnight, most emerging market currencies are heading weaker on the day due to the risk-off sentiment.

Key Global Financial Indicators

Last updated: 2/7/19 8:19 AM	Level		Change from Market Close				
	Last 12m	Latest	1 Day	7 Days	30 Days	12 M	YTD
Equities					%		%
S&P 500		2732	-0.2	2	7	2	9
Eurostoxx 50		3177	-1.1	1	5	-8	6
Nikkei 225		20751	-0.6	0	4	-4	4
MSCI EM		43	-1.0	0	8	-10	10
Yields and Spreads					bps		
US 10y Yield		2.66	-0.4	4	-3	-17	-2
Germany 10y Yield		0.12	-4.1	-3	-10	-62	-12
EMBIG Sovereign Spread		351	24	-15	-52	61	-63
FX / Commodities / Volatility					%		
EM FX vs. USD, (+) = appreciation		63.7	-0.2	-1	1	-10	2
Dollar index, (+) = $ appreciation		96.5	0.1	1	1	7	0
Brent Crude Oil ($/barrel)		62.2	-0.8	0	8	-5	16
VIX Index (%, change in pp)		16.3	0.9	0	-5	-11	-9

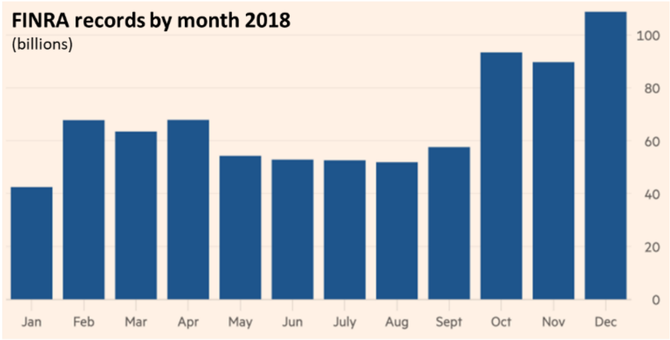
Colors denote tightening/easing financial conditions for observations greater than ±1.5 standard deviations. Data source: Bloomberg.

United States

back to top

Stocks weakened Wednesday in light trade. The S&P 500 fell for the first time in six sessions. Market sentiment still remains clouded by the prospect of another government shutdown and trade concerns. Mixed earnings coming to market also contributed to a choppy session. Treasury yields ended little changed. Miami-based MIAX Options plans to begin trading a new volatility index called SPIKES on the 19th. This would be a competitor to the popular VIX index of implied volatility on the S&P 500.

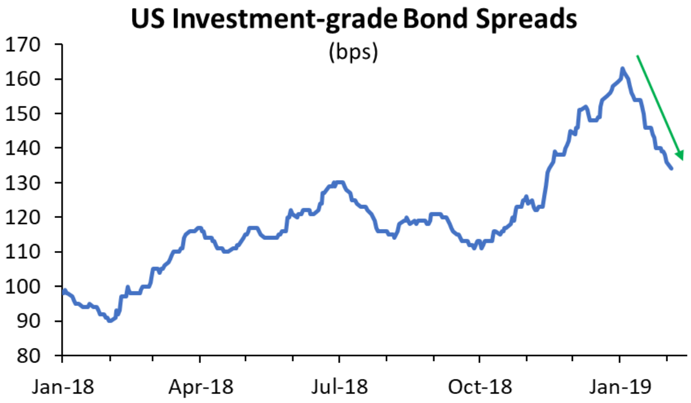
The average daily volume of electronic records hit a record high last year according to the Financial Industrial Regulatory Authority (FINRA). The financial sector watchdog reported that average daily volumes hit 66.7 bn in 2018, up 87% from the year before—and that volumes accelerated toward the end of the year. The Financial Times reported the increase stemmed from increased volatility, driven by heightened anxiety over a number of issues: the health of the global economy, US-China trade tensions, and the Fed hiking regime. FINRA advised that "the story of 2018 was not just individual, breakthrough days that saw new records—it was also the sustained, high-volume activity that we managed for days and even weeks at a time."



Source: FINRA; Financial Times

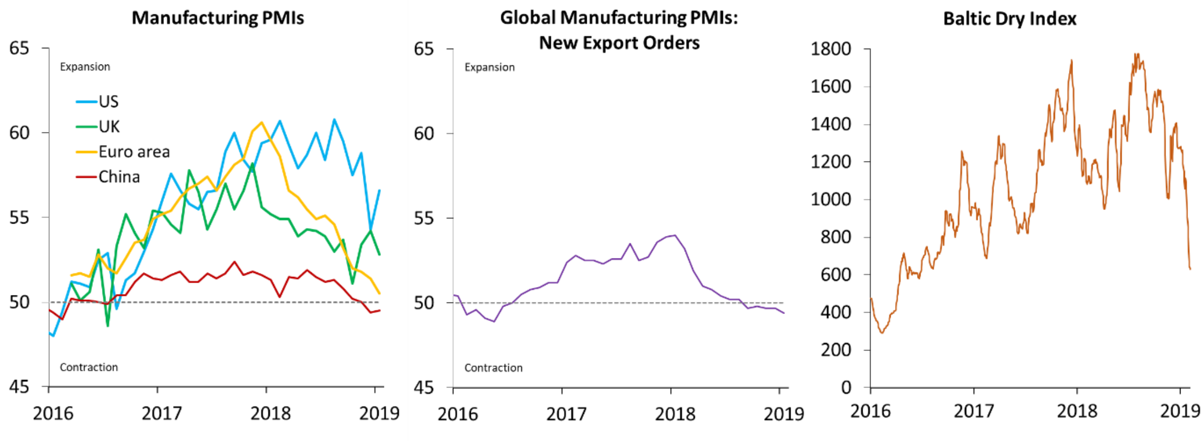
Public pension plans suffered considerable losses of 7.5% in Q4. They are now down around 5% since the beginning of the fiscal year according to Bloomberg, and may require state and local governments to make higher contributions or cut benefits to keep from losing ground. Moody's advises that a 10% loss in plan values would raise government funding costs by 35% in FY2030 just to "tread water."

Demand for investment-grade corporate bonds continues to strengthen this year. A Verizon issue this week was eight times oversubscribed and a New Jersey utility six times according to Bloomberg. And demand has been picking up in the secondary market too, with spreads falling since January 3rd. This follows a year where corporate bonds had their worst performance in a decade.



Source: Bloomberg, ICE Bank of America Merrill Lynch

The US trade deficit narrowed (-49.3 bn) in November. Bloomberg analysts speculate this was driven by a 2.9% fall in imports, which had been rising earlier as many consumers and businesses were front-loading their foreign purchases to get ahead of higher tariffs. Higher tariffs are due to begin in March 2nd, but there is increasing optimsim of a US-China trade deal before then. Concerns about global trade have continued. Recent data has helped spur these concerns, such as the fall-off in manufacturing sector PMIs, with China dipping below 50 (evidencing contraction) for a second straight month. And a new portion of JP Morgan's global manufacturing PMI breaking out exports has been tracking below 50 for five consecutive months now. Also, the Baltic Dry Index (a popular proxy for dry bulk shipping stocks) has been falling sharply over the past several months.



Source: Bloombeg, ISM, JP Morgan, Markit

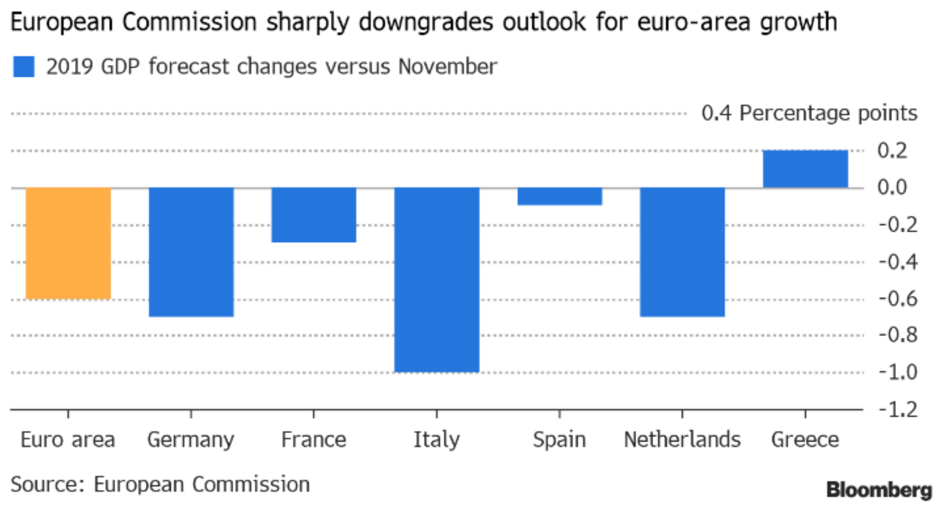
Europe

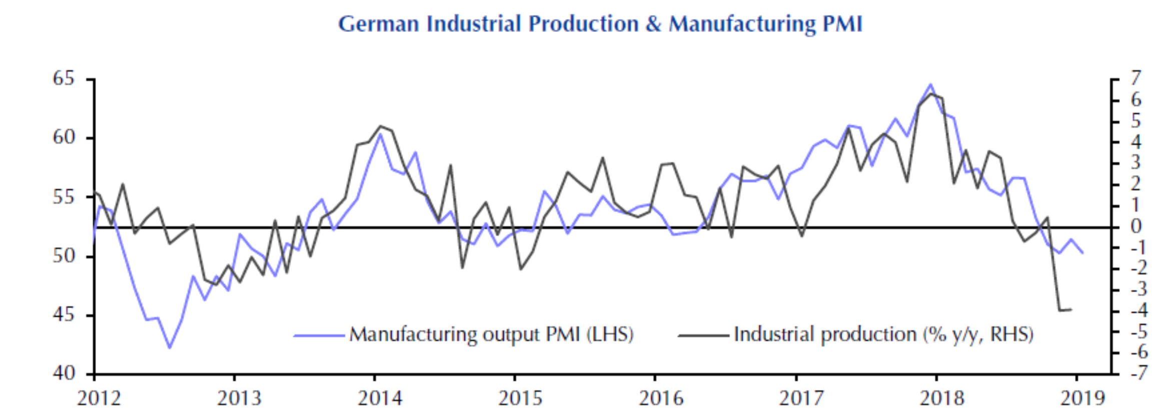
back to top

European bourses slipped this morning following the EC's publication of lower growth forecasts (see below). The DAX (-0.9%) and Titans 30 (-1.1%) suffered the largest losses as Germany and Italy were the countries with the largest downward revisions. Bank stocks (-0.9%) also dropped.

Euro area sovereign bond markets are mixed, with German 10-year bund yields dropping 4 bps to 0.12% while Italian bonds gain 8 bps to 2.93%, pushing the Germany-Italy spread to 283 bps. Moves for the yields of other European sovereigns have been smaller.

The European Commission (EC) has slashed its growth forecasts of all major economies in the eurozone. For the block, the EC has downgraded 2019 growth to 1.3%, from 1.9% in November. Growth for 2020 was also clipped by 0.1 p.p. to 1.6%. By country, the largest growth revisions are for Italy (-1 p.p), Germany (-0.7 p.p), and the Netherlands (-0.7 p.p). Separately, **Germany's Industrial Production disappointed in December** with a 0.4% monthly fall compared to a +0.7% expected increase. On an annual level, German IP was 3.9% lower than a year ago.

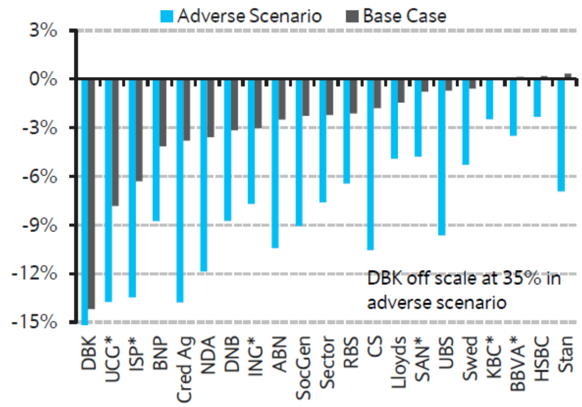




Sources: Thomson Reuters, Markit

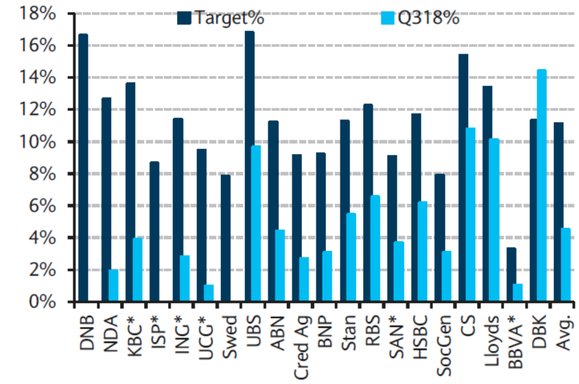
ECB's 2019 supervisory stress test will focus on bank liquidity risk. The ECB announced that its 2019 supervisory stress test will focus on banks' liquidity outflows under adverse and extreme shock scenarios to estimate each bank's expected short-term cash outflows and the 'survival period' over which the bank can operate with available cash and collateral but no access to funding markets. The ECB has positioned this exercise as a tool to identify needed improvements in banks' liquidity management, specifying that it will feed into the Supervisory Review and Evaluation Process (SREP) but will not directly affect bank capital or liquidity requirements. The last ECB stress test, in 2017, focused on the impact of interest rate changes. This year's focus on liquidity stress is consistent with increasing concern over banks' potential funding stress (see below) that has prompted widespread discussion over possible measures, mainly extensions of targeted long-term refinancing operations (TLTRO), to ameliorate bank liquidity and funding risk.

Funding Cost Scenario Impact on 2019 Profit Before Tax (Percent)



Source: Barclays Research,* not covered by Barclays. For these stocks consen: PBT is used, sourced from Refinitiv on 21/01/19.

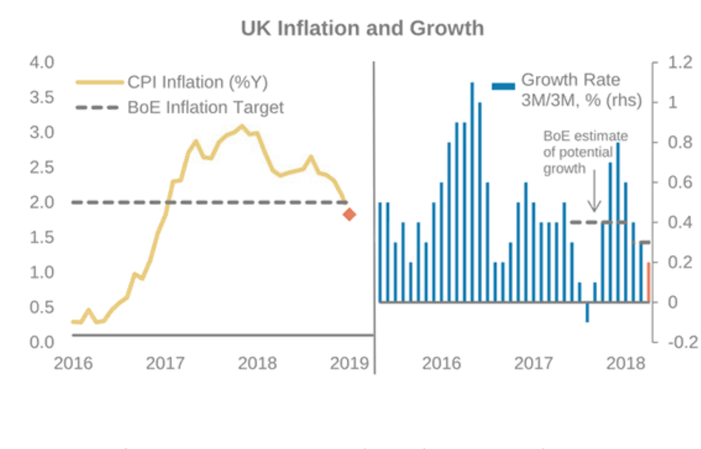
MREL-qualifying Senior Debt, Current and Target (% of Risk-Weighted Assets)



Source: Company Disclosure, Barclays Research. * not covered by Barclays, ** Q318 RWAs adjusted for assumed Basel 4 impact

On **Brexit news**, as PM May heads to Brussels for last-minute negotiations to avoid a no-deal exit, local newspapers speculate the new vote on the Withdrawal Agreement (WA) will be postponed to the week of February 25. Opposition leader Jeremy Corbyn has laid out his party's five requirements to support the WA. Namely, (i) a "permanent and comprehensive UK-wide customs union"; (ii) close alignment with the EU's single market, underpinned by "shared institutions"; (iii) "dynamic alignment on rights and protections", so that UK standards do not fall behind those of the EU; (iv) clear commitments on future UK participation in EU agencies and funding programs; and (v) unambiguous agreements on future security arrangements. As the political rhetoric gets increasingly toxic, EU leaders have continued to affirm that the WA will not be renegotiated.

The Bank of England has left its policy parameters unchanged, as expected. The MPC voted unanimously to maintain the Bank Rate at 0.75% and the pace of asset purchases at £10 bn and £435 bn for the Corporate Bond and Asset Purchase programs. The Committee noted that uncertainty has intensified, largely due to Brexit, and thus has downgraded its growth forecast for 2019 to 1.2% (from 1.7%). The BoE also noted that this growth forecast would have to be revised once there was greater clarity on the final Brexit arrangement. At the press conference, governor Carney underscored the risks to the UK economy stemming from "the fog of Brexit" and noted that household spending is unlikely to remain as resilience as in the past given the current large uncertaiinnty. **The pound is 0.4% weaker to the dollar at $1.29 and 10-year gilt yields dropped 5 bps to 1.16%.**



UK property funds suffered sizeable outflows in December 2018, according to the FT. Real estate funds saw redemptions of around £315m last December, comparable to outflows of £466m and £328m seen in June and July of 2016 in the aftermath of the Brexit referendum. The Financial Conduct Authority has reportedly instructed real estate investment funds to report daily on their liquidity situation

Other Mature Markets back to top

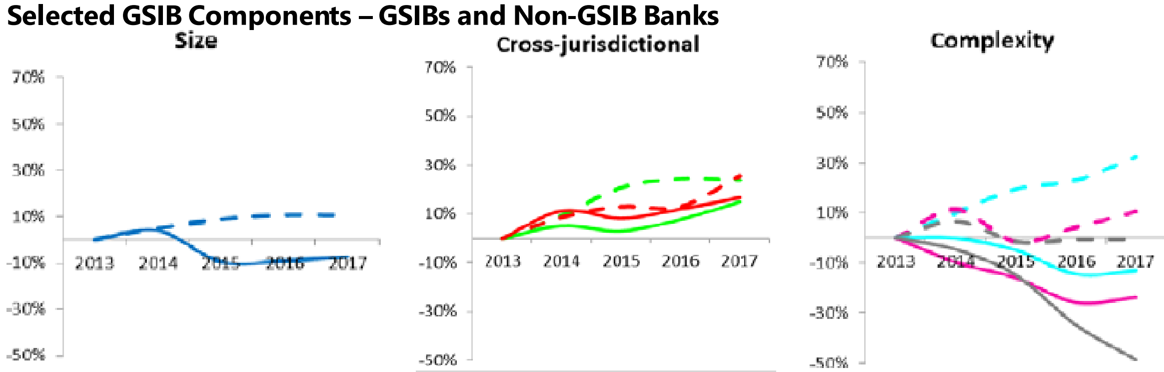
Japan

Equities declined (Topix -0.8%; Nikkei -0.6%) on disappointing earnings. Index performance was flattered by a surge in Softbank (+18%) after announcing plans to buy back shares worth 10% of its market value. Softbank plans to fund the buyback with the proceeds of the IPO of its mobile unit last year. **Yields on 10-year JGBs rose 0.8 bps to -0.021%. The yen was little changed.**

Global Systemically Important Banks (GSIBs)

New empirical study suggests GSIBs are behaving consistent with the capital surcharge framework. A new working paper indicates that the Basel Committee's framework to identify and impose capital surcharges on GSIBs is broadly generating the intended behavioral and systemic risk outcomes. GSIBs' degree of systemic importance (on a measure that includes size, interconnectedness, cross-jurisdictional reach, market risk exposures and role in the global financial infrastructure) has declined, particularly for U.S., U.K. and European banks. (Japanese and Chinese banks' GSIB scores have risen.) GSIBs' declining scores have resulted mainly from a dramatic decrease in their "complexity" (a measure that captures holdings of market-sensitive and illiquid exposures characteristic of markets activities; see below) and in their "interconnectedness" (which includes interbank assets and liabilities and securities outstanding). GSIBs' have retrenched little or not at all on other key attributes, such as total size and cross-border orientation. A second major finding is that GSIB-like characteristics and activities has migrated to non-GSIB banks – a shift congruent with the intention to dilute "too big to fail" risks.

Selected GSIB Components – GSIBs and Non-GSIB Banks



Note: Solid lines represent GSIBs; dotted lines are for a group of non-GSIBs. "Cross-jurisdictional" includes cross-border claims (green) and liabilities (red). Complexity includes OTC trading (light blue), AFS (violet) and Level 3 (gray) assets.

Source: Basel Committee on Banking Supervision. "An examination of initial experience with the global systemically important bank framework." Working Paper 34. https://www.bis.org/bcbs/publ/wp34.htm

Emerging Markets back to top

Asian stocks were overall little changed on net (+0.1%) with Greater China markets still closed for holidays. Asian currencies traded little changed against the dollar: the Malaysian ringgit gained the most (+0.5%), while the Korean won and the Indonesia rupiah posted the largest depreciation (-0.4%). **Equities in EMEA were moderately lower this morning, with South Africa (-1.1%) the worst performer of the major markets.** Local currencies were slightly weaker against the dollar. **Latin American equities dropped** yesterday on increased trade risks, particularly in Brazil (-3.7%) where the central bank provided no forward guidance. Major regional currencies were 0.4%-0.8% weaker. Local government bond yields were mostly little changed, except Brazil (+11 bps).

Key Emerging Market Financial Indicators

Last updated: 2/7/19 8:17 AM	Level Last 12m	index	Change 1 Day	7 Days	30 Days	12 M	YTD
Major EM Benchmarks					%		%
MSCI EM Equities		42.83	-1.0	0	8	-10	10
MSCI Frontier Equities		28.32	-0.9	0	5	-16	8
EMBIG Sovereign Spread (in bps)		350	23	-16	-53	60	-64
EM FX vs. USD		63.69	-0.2	-1	1	-10	2
Major EM FX vs. USD					**%, (+) = EM currency appreciation**		
China Renminbi		6.75	0.0	-1	2	-7	2
Indonesian Rupiah		13973	-0.4	0	1	-3	3
Indian Rupee		71.46	0.2	-1	-2	-10	-2
Argentine Peso		37.73	-0.5	-1	-1	-48	0
Brazil Real		3.72	-0.5	-2	0	-12	4
Mexican Peso		19.17	-0.3	0	1	-2	3
Russian Ruble		66.05	-0.3	-1	1	-12	5
South African Rand		13.63	-0.7	-3	2	-11	5
Turkish Lira		5.26	-0.9	-2	2	-28	0
EM FX volatility		8.90	0.0	0.1	-0.5	0.0	-0.9

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

India

The Reserve Bank of India (RBI) unexpectedly cut the policy rate by 25 bps to 6.25%. At the first policy meeting of the new RBI governor, Shaktikanta Das, the MPC voted 4-2 in favour of reducing the policy rate and voted unanimously to change its policy stance back to "neutral" from "calibrated tightening". Headline inflation slowed to 2.2% y/y in December, well below the RBI's target of 4%, but core inflation remained elevated at 5.7%. The RBI also lowered its inflation and growth forecasts for 2019 and 2020. Yields on Indian 10-year government bonds fell 5 bps, equities gained 0.3%, and the rupee appreciated 0.2%. Separately, **the RBI plans to remove a restriction that limits a foreign investor's exposure to a single company to 20% of its total investments in corporate bonds in India.** Analysts saw the move as an attempt to encourage more foreign inflows into corporate bonds.

Brazil

The central bank left its policy rate unchanged at 6.50%, as widely expected. The MPC kept its policy rate on hold at a record low level in a unanimous decision and acknowledged that the balance of risk for inflation has improved. However, it maintained that inflation risk is skewed to the upside and provided no forward guidance. Given lower-than-expected inflation (table) and worrisome signals about demand from a weakening labor market, some expected an easing bias from the central bank. The equity market sold off sharply ahead of the monetary decision, losing 3.7% yesterday, and the 10-year government bond yield jumped 11 bps.

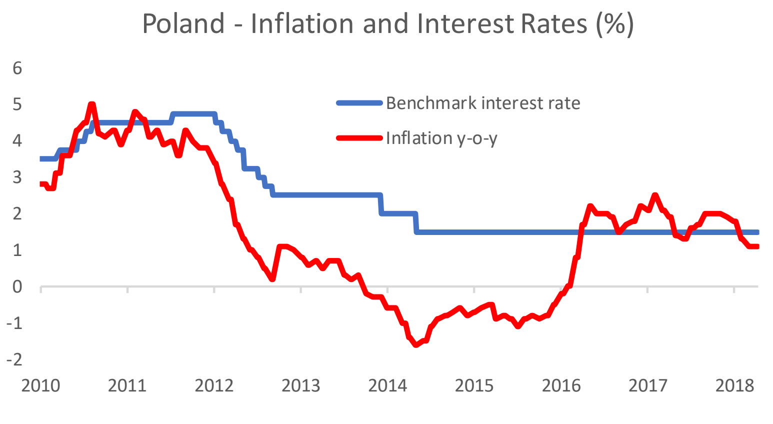
Inflation Forecasts: Evolution Since Dec. Meeting

	Feb. 6, 2019 2019	2020	Dec. 12, 2018 2019	2020
BCB Forecasts, assuming FX and interest rates stable at pre-meeting levels				
Selic, year-end	6.5% ↔	6.5% ↔	6.5%	6.5%
BRL, year-end	3.70 ↓	3.70 ↓	3.85	3.85
IPCA Inflation, YoY	3.9% ↓	4.0% ↔	4.0%	4.0%
BCB Forecasts, assuming consensus FX and interest rate path				
Selic, year-end	6.5% ↓	8.0% ↔	7.5%	8.0%
BRL, year-end	3.70 ↓	3.75 ↓	3.80	3.80
IPCA Inflation, YoY	3.9% ↔	3.8% ↑	3.9%	3.6%
Focus Survey				
Market Consensus IPCA	3.9% ↓	4.0% ↔	4.1%	4.0%

Source: BCB

Poland

The zloty weakened slightly after the central bank sounded a dovish tone at yesterday's meeting. The bank's headline interest rate was kept unchanged at 1.5%, as unanimously expected. Governor Glapinski confirmed that the policy stance would remain the same for some time, and that the bank doesn't "need to consider any changes in our monetary policy". This follows recent remarks that the rate could be kept at its current level until 2022. Glapinski also suggested to reporters yesterday that the Federal Reserve had been too aggressive in tightening policy and that "they admit now that they made a mistake". The zloty has weakened by 0.3% since the meeting to just above 4.3 against the euro.



Source: Bloomberg

Philippines

Bangko Sentral ng Pilipinas (BSP) kept its policy rate on hold at 4.75%, as widely expected. The central bank marginally tweaked its inflation forecast downwards and said that it expects headline inflation to be back within target by March. Notable was a shift in BSP's focus on liquidity conditions with a Deputy Governor saying that a planned retail bond offering by the government "could lead to tightening liquidity". Excess liquidity parked at the BSP has fallen to its lowest level in years. Yields on 10-year government paper surged 11 bps to 6.2% on the planned retail bond offering. Stocks gained 0.5% and the peso was unchanged.

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Global Financial Indicators

Last updated: 2/7/19 8:20 AM	Level		Change				YTD
	Last 12m	Latest	1 Day	7 Days	30 Days	12 M	
Equities				%			%
United States		2732	-0.2	2	7	2	9
Europe		3177	-1.1	1	5	-8	6
Japan		20751	-0.6	0	4	-4	4
China		2618	1.3	1	4	-24	5
Asia Ex Japan		69	-0.9	1	8	-9	9
Emerging Markets		43	-1.0	0	8	-10	10
Interest Rates				basis points			
US 10y Yield		2.66	-0.4	4	-3	-17	-2
Germany 10y Yield		0.12	-4.1	-3	-10	-62	-12
Japan 10y Yield		-0.01	0.5	-1	0	-8	-1
UK 10y Yield		1.18	-3.3	-4	-7	-37	-9
Credit Spreads				basis points			
US Investment Grade		119	0.0	-5	-30	37	-28
US High Yield		423	3.9	-15	-55	79	-98
Europe IG		73	2.8	2	-13	25	-15
Europe HY		316	9.0	8	-29	66	-37
EMBIG Sovereign Spread		351	24.0	-15	-52	61	-63
Exchange Rates				%			
Dollar Index (DXY)		96.51	0.1	1	1	7	0
USDEUR		1.13	-0.2	-1	-1	-8	-1
USDJPY		109.7	0.3	-1	-1	0	0
EM FX vs. USD		63.7	-0.2	-1	1	-10	2
Commodities				%			
Brent Crude Oil ($/barrel)		62	-0.8	0	8	-5	16
Industrials Metals (index)		119	-0.2	1	7	-11	9
Agriculture (index)		43	-0.4	1	1	-11	3
Implied Volatility				%			
VIX Index (%, change in pp)		16.3	0.9	-0.3	-5.1	-11.4	-9.1
10y Treasury Volatility Index		3.7	0.1	-0.1	-0.8	-1.5	-0.9
Global FX Volatility		7.8	0.0	0.0	-0.9	-0.8	-1.2
EA Sovereign Spreads				10-Year spread vs. Germany (bps)			
Greece		384	10.2	12	-32	90	-32
Italy		281	10.8	37	13	160	31
Portugal		154	3.8	7	-6	27	6
Spain		112	2.4	7	-16	45	-6

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)						
2/7/2019	Level		Change (in %)					Level		Change (in basis points)				
8:20 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		6.75	0.0	-0.7	2	-7	2		3.1	0.0	-2	-4	-91	-13
Indonesia		13973	-0.4	0.0	1	-3	3		7.9	-7.2	-41	-30	127	-26
India		71	0.2	-0.5	-2	-10	-2		7.6	-3.7	3	7	-20	13
Philippines		52	0.2	-0.1	0	-2	1		5.7	-0.9	-4	-60	97	-59
Thailand		31	0.1	0.0	2	1	4		2.6	-0.3	-3	1	24	-6
Malaysia		4.07	0.5	0.6	1	-4	2		4.0	0.0	-2	-4	2	-7
Argentina		38	-0.5	-1.1	-1	-48	0		20.8	30.2	-46	-141	537	-222
Brazil		3.72	-0.5	-1.9	0	-12	4		7.8	4.6	-14	-21	-102	-36
Chile		655	0.0	0.0	4	-9	6		4.4	-0.2	-8	-2	-45	-8
Colombia		3114	-0.3	-0.2	2	-9	5		6.4	-1.0	-12	-17	9	-12
Mexico		19.17	-0.3	-0.3	1	-2	3		8.4	0.3	-12	-4	76	-29
Peru		3.3	0.0	0.9	1	-2	1		5.6	1.1	-15	-13	78	-13
Uruguay		32	0.0	0.2	0	-12	0		10.3	1.5	-12	-43		-46
Hungary		281	-0.4	-2.0	-1	-10	-1		2.0	-3.1	-14	-15	25	-23
Poland		3.79	-0.3	-1.8	-1	-10	-1		2.2	-0.4	-1	-7	-52	-4
Romania		4.2	-0.2	-1.0	-3	-9	-3		4.3	-5.0	-13	18	29	4
Russia		66.0	-0.3	-1.0	1	-12	5		7.9	1.7	-12	-47	94	-46
South Africa		13.6	-0.7	-2.8	2	-11	5		9.4	3.8	-8	-7	23	-23
Turkey		5.26	-0.9	-1.9	2	-28	0		15.2	13.3	-26	-192	337	-165
US (DXY; 5y UST)		97	0.1	1.0	1	7	0		2.47	-3.7	3	-7	-9	-4

	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		2618	0.0	1	4	-24	5		184	11	-3	-1	18	-10
Indonesia		6536	-0.2	1	4	0	6		192	22	-5	-35	21	-44
India		36971	0.0	2	3	8	3		174	0	-12	-20	70	-22
Philippines		8100	0.5	2	4	-7	8		89	39	-9	-21	-29	-32
Malaysia		1693	1	0	1	-9	0		132	7	-8	-24	23	-30
Argentina		36732	-2.0	2	11	16	21		669	36	-2	-48	252	-146
Brazil		95389	-3.7	-2	4	15	9		241	26	6	-13	-5	-32
Chile		5432	-0.7	0	5	-6	6		139	19	-8	-15	19	-27
Colombia		1489	-0.3	3	10	-2	12		192	28	2	-12	7	-36
Mexico		43856	-1.1	0	2	-10	5		315	25	-15	-17	71	-39
Peru		20533	0	2	5	0	6		141	28	-3	-18	-9	-27
Hungary		40113	-1.2	-2	-1	1	2		111	15	-27	-26	14	-37
Poland		60425	-1.4	0	2	-4	5		54	2	-16	-14	-1	-31
Romania		7557	1.5	9	-2	-6	2		192	-1	-28	-22	78	-29
Russia		2511	-1.1	0	4	11	6		220	20	-4	-20	53	-32
South Africa		53705	-1.6	-1	3	-6	2		288	26	-22	-63	50	-77
Turkey		102303	-0.2	-2	14	-11	12		394	35	-18	-48	92	-35
Ukraine		557	0.1	1	1	67	0		685	38	-12	-127	268	-102
EM total		43	-1.0	0	8	-10	10		350	23	-16	-53	60	-64

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