GLOBAL MARKETS ANALYSIS
Monetary and Capital Markets

Global Markets Monitor

TUESDAY, FEBRUARY 8, 2022

- **US yield curve flattens ahead of Fed rate hike cycle** (link)
- **Hawkish Fed drives US yields higher at the long end** (link)
- **Japanese 10-year yields rise to test central bank target** (link)
- **China relaxes lending standards to boost affordable housing** (link)
- **Ghana credit spreads balloon on Moody's downgrade** (link)
- **Special Feature: ESG Monitor** (attached)

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Rising interest rates test global markets

Interest rates continued their ascent, with the global benchmark US Treasury bond yield approaching 2%, a level it has not seen since 2019. In Japan, the bond market has come back to life after years of quiescence with the 10-year Japanese Government Bond (JGB) yield hitting its highest level since 2015 and testing the Bank of Japan's 0.25% yield target. 10-year bund yields are at their highest since 2019, and gilt yields are also pushing higher. The hawkish turns by the Fed, ECB and BOE have triggered a new phase for global markets in which policy rate hikes and higher interest rates are the new reality. Elsewhere, hopes for progress with the Ukraine situation propped up local markets, but globally stocks were mixed with low trading volumes. Meanwhile, crypto assets have started another rally, with Bitcoin up 14% for the month even though technology stocks have lost ground so far in February.

Key Global Financial Indicators

Last updated: 2/8/22 7:36 AM	Level: Last 12m	Level: Latest	Change from Market Close: 1 Day	7 Days	30 Days	12 M	YTD
Equities					%		%
S&P 500		4484	-0.4	-1	-4	15	-6
Eurostoxx 50		4114	-0.2	-3	-4	12	-4
Nikkei 225		27285	0.1	1	-4	-8	-5
MSCI EM		49	-0.2	-1	-1	-14	-1
Yields and Spreads					bps		
US 10y Yield		1.94	2.7	16	18	77	43
Germany 10y Yield		0.23	0.2	19	27	68	41
EMBIG Sovereign Spread		381	5	-3	14	44	14
FX / Commodities / Volatility					%		
EM FX vs. USD, (+) = appreciation		53.3	0.1	0	1	-8	1
Dollar index, (+) = $ appreciation		95.6	0.2	-1	0	5	0
Brent Crude Oil ($/barrel)		90.8	-2.1	2	11	50	17
VIX Index (%, change in pp)		23.3	0.4	1	5	2	6

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

Mature Markets

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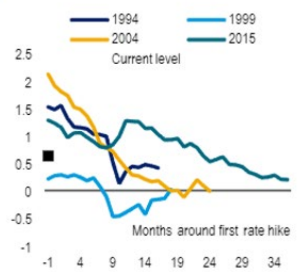
United States

Markets are treading a well-worn path as the US yield curve flattens ahead of the upcoming Fed rate hike cycle. The curve flattened ahead of each of the four previous Fed cycles. The hawkish shifts from the ECB and BOE should give the Fed some cover to be more aggressive, according to analysts at Bank of America. In the 2015 cycle, low yields in other advanced economies limited the Fed's ability to keep hiking rates, so this time rate hikes by other advanced economy central banks means that the impact of higher policy rates and interest rates more generally will be mitigated by matching rises overseas. This could also limit the appreciation of the dollar relative to other currencies, removing one potential macroeconomic headwind. Meanwhile, financial conditions in the US remain very loose by historical standards, a further spur to more aggressive Fed policy.

Exhibit 3: 2s10s curve during hiking cycle
2s10s curve typically flattens during hiking cycle



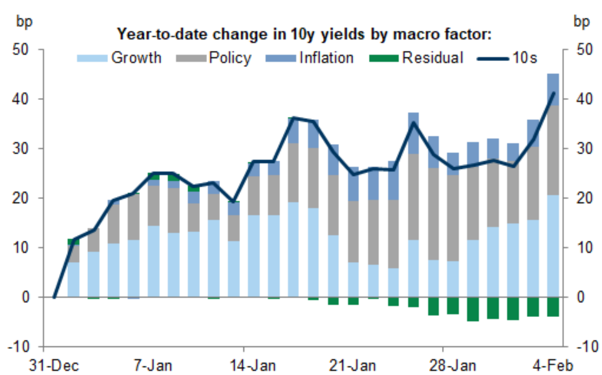
Source: BofA Global Research, Bloomberg
BofA GLOBAL RESEARCH

Exhibit 5: Bloomberg FCI
Values >0 indicate more accommodative conditions versus pre- financial crisis period, conditions are still relatively accommodative

Source: BofA Global Research, Bloomberg
BofA GLOBAL RESEARCH

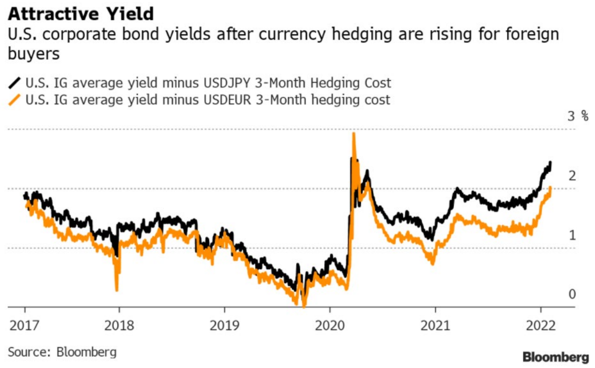
The Fed's hawkish turn is now the main driver of changes in 10-year Treasury yields, according to research by Goldman Sachs. Other factors such as growth and inflation have had a waning impact in recent weeks. 10-year yields have consistently been setting higher lows in recent trading, and the Goldman analysts think the rise in rates at the front end of the yield curve sets the stage for further increases at the long end. With the entire yield curve with the exception of the two-year Treasury back above pre-pandemic yield levels, most contacts expect the 10-year yield to break the psychologically important 2% level in the near future, a level not seen since 2019. Position data from the US Commodities and Futures Trading Commission (CFTC) show that futures investors have large short positions in 10-year and 30-year Treasury futures. The 10-year yield is up 40 bps since the start of the year and more than 55 bps since the beginning of December.

Yield repricing has become increasingly policy-driven
Cumulative year-to-date change in 10y UST yields by macro factor



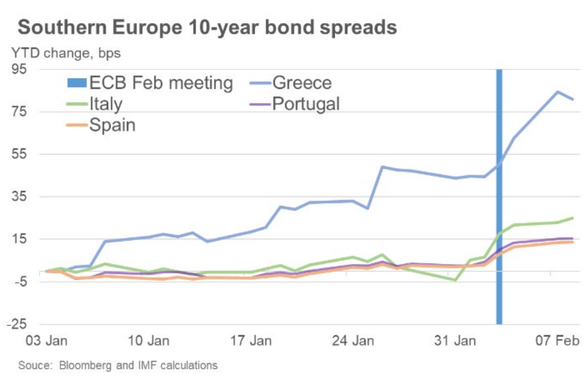
Source: Goldman Sachs Global Investment Research

The hawkish shift in global central bank policy could boost the US corporate bond market through increased purchases by foreign investors, according to JP Morgan and Bloomberg analysts. The rise in interest rates has pushed the yield on the Bloomberg US Corporate bond index to 2.93%, the highest since April 2020. In addition, the hawkish turn by the Fed and BOE has pushed interest rates higher in the euro area and the UK, making hedging costs for non-dollar investors cheaper. Rising interest rates in Japan presents the same opportunity to yen based investors, the analysts argue. The end of recent dollar strength also keeps hedging costs down, with the euro up for the year and the yen holding steady after both currencies weakened against the dollar last year. Other analysts disagree, taking the view that higher local yields are likely to make domestic markets more attractive to these investors. They also point out that the uncertainties surrounding the Fed's quantitative tightening policy could also deter investors.



Euro Area

In what some analysts see as a subtle push-back on market pricing, ECB President Lagarde stressed that any policy adjustment would be gradual, noting the importance of remaining data-dependent, and of maintaining flexibility and optionality. President Lagarde noted the ECB will use any instrument to ensure policy is transmitted to all member states. These comments were largely echoed this morning by ECB Governing council member Pablo Hernandez de Cos. **This morning the German 10-yr bund yields were little changed trading at around 0.22%, while southern spreads generally tightened although Italian spreads underperformed (+2 bps).**



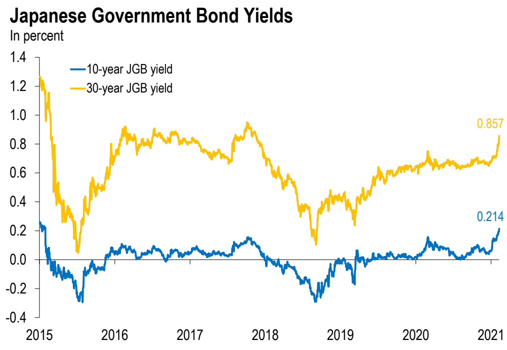
Markets now price roughly 45 bps of ECB hikes by December 2022, compared to over 50 bps at the end of last week. Analysts have divergent views about ECB policy this year, with several expecting the ECB to end net asset purchases in August and hike interest rates by 25 bps each at the September and December meetings. Several analysts expect this to be followed by an additional 75 bps of hikes in 2023.

European energy prices increased after Electricite de France (EDF) cut its nuclear power production forecast for this year. The German forward curve prices for 2023 increased by 4.2% while the French contract for next year increased by 7%. Dutch natural gas prices one month ahead (+3.8%) were also trading higher this morning following reports that U.S. President Joe Biden said that the Nord Stream 2 natural gas pipeline between Russia and Germany would be stopped if President Vladimir Putin orders an invasion of Ukraine.

The euro was trading weaker (-0.3%), reversing some of the gains seen at the start of the month. Analyst generally see further support for the currency, but some contacts flag that wider sovereign spreads could be a headwind to euro strengh. Goldman Sachs analysts think the euro is currently undervalued agains the dollar while. In other news, analysts anticipate that the negative impact of higher yields on the debt sustaintability of highly indebted countries would be offset by an expanding economy. **Bloomberg surveys see median Q4 GDP for the eurozone at 4.7%, with Greece seen at 8.2% and Italy at 6.3%.**

Japan

JGB yields increased again as markets continued testing the Bank of Japan (BOJ)'s tolerance (10-year: +2.0 bps; 30-year: +3.5 bps). The benchmark 10-year yield rose to 0.214%, a new high since early 2015, closer to the BOJ's upper limit at 0.25% under its current policy framework. Analysts noted that as the yield approaches the 0.25% mark, the BOJ could boost scheduled purchases, conduct unscheduled purchases (the last intervention was in March 2020), or secure an unlimited amount of bonds at a fixed rate (like in July 2018). Meanwhile, the sale of inflation-linked bonds drew strong demand, with a bid-to-cover ratio at the highest level since June 2007, as market participants expect to see higher inflation in Japan.



Emerging Markets

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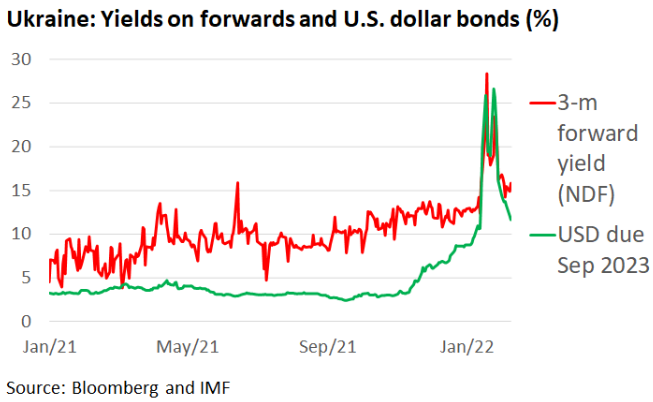
EMEA stocks were higher as currencies traded without much direction. The ruble was little changed but Russian equities (1.4%) outperformed and yields on Ukrainian Eurobonds fell as contacts argued that a meeting between Russian President Putin and French President Macon signals further de-escalation.

U.S. President Biden also warned that the Nord Stream 2 project would be stopped if Russia invades Ukraine. **Asian stocks lost ground, as did many currencies.** Citi analysts predicted that the inclusion of Indian debt in global bond indexes will not occur this year. **Latin American equities surged, although currencies were mixed.**

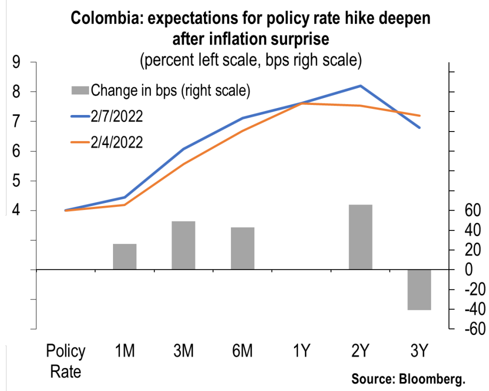


China and Hong Kong SAR

China eased bank lending standards to fund affordable rental housing projects. Such lending will no longer be subject to regulatory limits. In January, the Ministry of Housing and Urban-Rural Development said that a total of 6.5 mn homes for leasing purposes will be built across 40 major cities in the five years through 2025, accounting for about 26% of new housing supply and benefiting 13 mn people. Analysts noted that the relaxation of lending standards for rental housing reflected Beijing's efforts to tackle a slumping property market and advance the common prosperity goal. Equities declined (CSI 300: -0.5%; Hang Seng China Enterprises (-0.9%). A selloff in the healthcare sector was led by Wuxi Biologics (listed in Hong Kong SAR) after the firm was one of 33 entities that were just added to the US Commerce Department's unverified list; firms on the list are not barred from doing business in the US but may need additional licenses to buy products from U.S. entities.

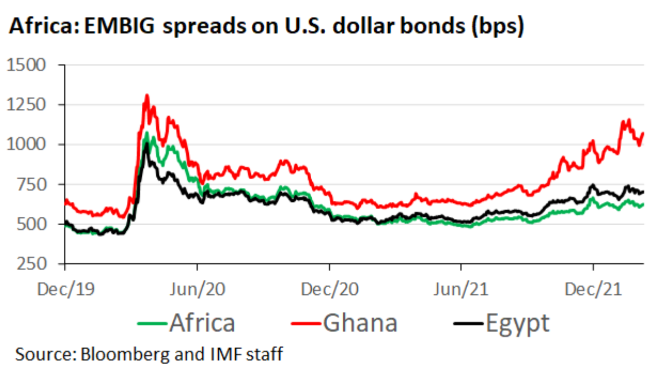
Colombia

An inflation surprise generated an emergency policy response and raised rate hike expectations. In the wake of a 55 bps higher than expected January inflation print of 6.9% yoy, Colombian authorities announced on Saturday a package of policy measures to address the challenge. These include lower import tariffs for agricultural goods, subsidies for an additional million families, additional credit lines to food producers, and logistical improvements in ports to lower costs. With core inflation climbing 1 ppt, to 3.9% yoy, analysts expect a weaker peso. The market-implied future monetary policy rate rose by 49 bps at the three-month horizon.



Ghana

The country's EMBIG U.S. dollar bond spreads rose above 1000 bps again after Moody's downgraded Ghana's credit rating from B3 to Caa1 with stable outlook. Moody's cited Ghana's increasingly difficult liquidity and debt challenges. Moody's also added that weak revenue generation constrains the government's budget flexibility, and that tight funding conditions in international markets have forced the government to rely on debt with shorter maturities. **Ghana reportedly plans to appeal the downgrade and argues that the decision to downgrade did not include material information such as the 2022 budget expenditure control measures, upfront fiscal adjustments, and inaccurate BOP statistics.** Moody's is the first rating agency to downgrade Ghana to the C category. Ethiopia, Gabon, Zambia, and Mozambique are other countries in the C-category across rating agencies.



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Global Financial Indicators

Last updated: 2/8/22 7:38 AM	Level		Change				
	Last 12m	Latest	1 Day	7 Days	30 Days	12 M	YTD
Equities					%		%
United States		4484	-0.4	-1	-4	15	-6
Europe		4115	-0.1	-3	-4	12	-4
Japan		27285	0.1	1	-4	-8	-5
China		4609	-0.5	-1	-4	-19	-7
Asia Ex Japan		81	-0.3	0	-2	-18	-2
Emerging Markets		49	-0.2	-1	-1	-14	-1
Interest Rates					basis points		
US 10y Yield		1.94	2.7	16	18	77	43
Germany 10y Yield		0.23	0.4	20	28	68	41
Japan 10y Yield		0.22	2.1	4	8	15	15
UK 10y Yield		1.45	4.6	15	28	98	48
Credit Spreads					basis points		
US Investment Grade		128	0.9	1	16	38	16
US High Yield		388	2.1	1	42	30	50
Europe IG		64	-1.8	6	13	17	17
Europe HY		313	-6.0	31	56	69	71
Exchange Rates					%		
USD/Majors		95.56	0.2	-1	0	5	0
EUR/USD		1.14	-0.2	1	1	-5	0
USD/JPY		115.4	0.2	1	0	10	0
EM/USD		53.3	0.1	0	1	-8	1
Commodities					%		
Brent Crude Oil ($/barrel)		91	-2.1	2	11	50	17
Industrials Metals (index)		184	0.2	2	6	35	6
Agriculture (index)		66	-0.5	0	6	28	8
Implied Volatility					%		
VIX Index (%, change in pp)		23.2	0.4	1.3	4.5	2.0	6.0
US 10y Swaption Volatility		80.0	1.1	1.7	-2.8	17.8	0.9
Global FX Volatility		7.5	0.0	0.2	0.3	0.3	0.1
EA Sovereign Spreads			10-Year spread vs. Germany (bps)				
Greece		224	-4.6	35	66	103	72
Italy		160	4.6	22	24	65	25
Portugal		78	-0.2	12	16	28	14
Spain		85	0.3	11	16	28	11

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

Last updated: 2/8/2022 7:47 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		6.37	-0.1	-0.1	0	1	0		2.8	1.0	5	-11	-59	-10
Indonesia		14399	0.0	-0.5	-1	-3	-1		6.5	1.0	6	5	29	12
India		75	-0.1	0.1	-1	-2	-1		6.3	0.0	0	9	75	0
Philippines		51	-0.2	-0.9	0	-7	-1		4.7	10.0	10	18	153	20
Thailand		33	0.1	0.7	2	-9	1		2.2	3.0	12	14	81	36
Malaysia		4.19	0.0	0.0	0	-3	0		3.7	1.4	4	5	90	13
Argentina		106	-0.3	-0.6	-2	-17	-3		49.9	11.5	41	88	39	-66
Brazil		5.26	-0.1	0.1	8	2	6		11.5	-0.4	21	4	350	82
Chile		822	0.4	-2.2	2	-11	4		6.1	38.5	44	21	323	67
Colombia		3964	-0.2	-0.5	2	-10	3		7.3	0.0	27	34	308	93
Mexico		20.68	-0.4	-0.7	-1	-3	-1		7.6	6.0	-2	-19	202	3
Peru		3.8	0.1	0.1	2	-5	4		6.1	0.2	-2	6	234	20
Uruguay		44	0.2	1.1	2	-3	2		8.6	-3.1	-22	-9	144	-16
Hungary		309	0.0	2.0	2	-4	5		4.6	-10.5	-27	-20	267	10
Poland		3.97	0.0	2.2	1	-6	2		3.9	-3.5	-17	-10	250	34
Romania		4.3	-0.2	1.4	1	-7	1		5.1	-0.2	3	4	278	24
Russia		75.2	0.3	2.2	0	-1	0		9.3	-2.5	-6	34	300	56
South Africa		15.5	0.2	-1.4	1	-4	3		7.7	-4.5	1	-18	100	23
Turkey		13.62	-0.2	-1.8	1	-48	-2		22.6	0.0	-39	-197	956	-174
US (DXY; 5y UST)		96	0.2	-0.8	0	5	0		1.79	2.8	18	29	132	53

	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	7 Days	30 Days	12 M	YTD
								basis points					
China		4609	-0.5	-1	-4	-19	-7		202	0	6	-22	-1
Indonesia		6790	-0.2	2	1	10	3		183	-3	20	5	18
India		57809	0.3	-2	-3	13	-1		145	6	21	-10	13
Philippines		7458	1.1	1	6	6	5		123	4	25	25	22
Malaysia		1530	0.0	1	-1	-4	-2		124	3	10	-12	7
Argentina		89189	1.4	-2	6	71	7		1779	61	-14	351	99
Brazil		111996	-0.2	0	9	-6	7		316	-6	1	59	5
Chile		4474	0.0	-3	4	0	4		157	2	19	16	17
Colombia		1534	0.7	0	10	11	9		363	-6	19	145	15
Mexico		51255	0.2	1	-4	16	-4		343	2	10	-4	11
Peru		22455	0.8	-2	0	2	6		172	7	15	43	22
Hungary		52724	1.3	0	1	19	4		137	8	24	-4	13
Poland		67552	0.7	-1	-5	18	-3		12	-1	-7	-17	-20
Romania		13395	0.1	0	2	25	3		210	6	25	20	17
Russia		3534	1.8	0	-6	3	-7		243	-32	68	70	66
South Africa		76143	0.6	2	3	17	3		374	8	33	13	19
Turkey		1991	-0.3	-1	-2	30	7		557	2	-19	135	-21
Ukraine		522	0.0	0	0	0	0		846	-45	73	381	87
EM total		49	-0.3	-1	-1	-14	-1		414	1	18	75	28

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

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