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- Inflation expectations in the euro-area ease ([link](#))
- Swedish Riksbank's capital hit by higher interest rates ([link](#))
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- Analysts expect a strong recovery in eurobond sales by emerging markets ([link](#))

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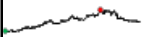
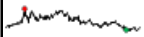

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US CPI bang on expectations

US Treasuries yields were choppy and the dollar weakened following the release of both a US core and headline CPI report for December bang on expectations. Earlier this morning, European bourses gained and US equity futures were steady ahead of the release. US Treasury yields were modestly lower and the dollar slightly weaker. Across the pond, euro-area government bond yields fell for the second consecutive trading day, particularly in Italy. Since yesterday's open, 10-year Italian yields have fallen 25 bps to 3.96%, with the spread to bunds narrowing to 180 bps, its lowest level since late April. The ECB's survey of inflation expectations showed a decrease, for the first time since May, but expectations remain well above the ECB 2% inflation target. Meanwhile, ECB officials have continued to convey a hawkish message. In emerging markets, equities rallied and most currencies strengthened. After Turkey sold \$2.75 bn in Eurobonds yesterday, and Romania earlier, analysts expect a sharp increase in the sale of dollar denominated bonds by emerging markets this year, even if issuance costs are relatively high versus history.

Key Global Financial Indicators

Last updated: 1/12/23 8:02 AM	Level		Change from Market Close				
	Last 12m	Latest	1 Day	7 Days	30 Days	12 M	YTD
Equities			%				%
S&P 500		3970	1.3	3	-1	-16	3
Eurostoxx 50		4133	0.8	4	5	-4	9
Nikkei 225		26450	0.0	3	-5	-7	1
MSCI EM		41	0.4	4	5	-20	8
Yields and Spreads			bps				
US 10y Yield		3.51	-3.1	-21	-10	177	-37
Germany 10y Yield		2.15	-5.3	-17	21	221	-42
EMBIG Sovereign Spread		462	-1	4	8	87	10
FX / Commodities / Volatility			%				
EM FX vs. USD, (+) = appreciation		51.0	0.1	2	2	-4	2
Dollar index, (+) = \$ appreciation		103.1	-0.1	-2	-2	9	0
Brent Crude Oil (\$/barrel)		83.9	1.5	7	8	-1	-2
VIX Index (% change in pp)		21.5	0.4	-1	-4	4	0

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

Mature Markets

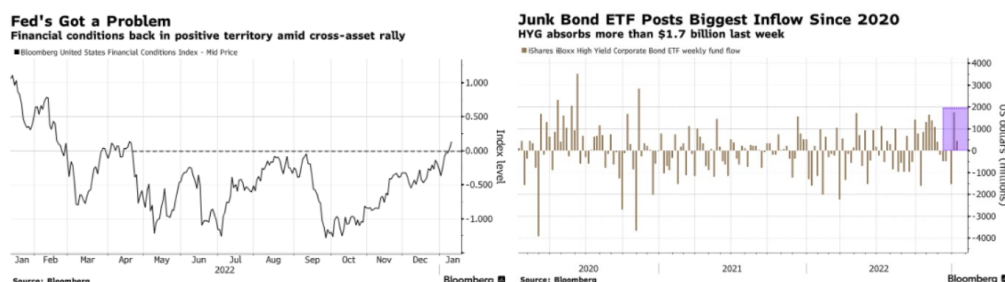
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United States

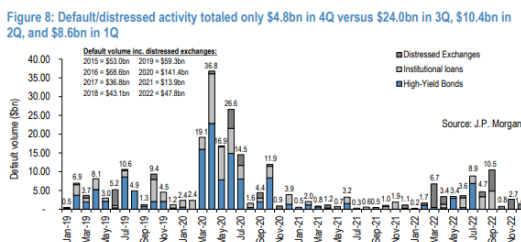
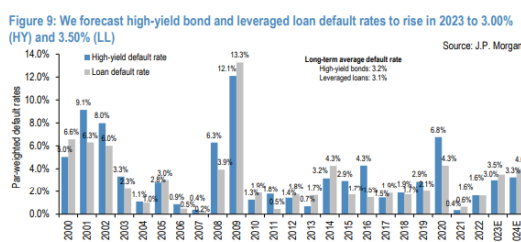
This morning, **both headline and core US CPI in December were exactly at expectations**: headline MoM -0.1%, YoY 6.5%; core MoM +0.3%, YoY 5.7%. Jobless claims were slightly below expectations: initial claims: 205k (vs exp. 215k); continuing claims: 1634k (vs exp. 1710k). The price action was choppy following the release.

Yesterday, the S&P 500 gained 1.3%, supported by those investors who expected that the US inflation print this morning would be softer and would trigger a risk-on price action for markets. US Treasury 10-year nominal yields dropped 8 bps, driven entirely by real yields.

The Bloomberg United States Financial Conditions Index turned positive, illustrating the Fed challenges to curb inflation (left chart below). The easing of financial conditions was backed by a rally across various risky assets as well as by surprisingly strong flows. In particular, flows into junk-bond funds were strong last week (right chart). The observed easing underpins recent Fed officials' comments that elevated policy rates should stay at high levels for longer throughout 2023.



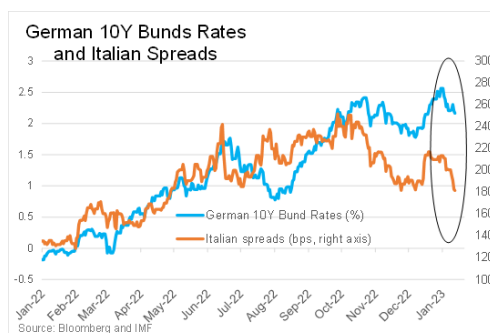
JP Morgan analysts expect a significant increase in default rates for high-yield bonds and leveraged loans in 2023 and 2024. The projected figures are 3.0% and 3.5% (bonds vs loans) in 2023, and 3.3% and 4.0% in 2024 (left chart below). It contrasts with almost a default-free 2021 (default rate 0.4–0.6%) and relatively mild 2022 (1.6%). The default rate projections are driven mostly by weak forecasted 2023 US GDP growth, risks of leveraged credit markets becoming more vulnerable to increased defaults with the passage of time amid sustained higher rates, constrained capital markets, and tight financial conditions weighing on fundamentals.



Euro Area

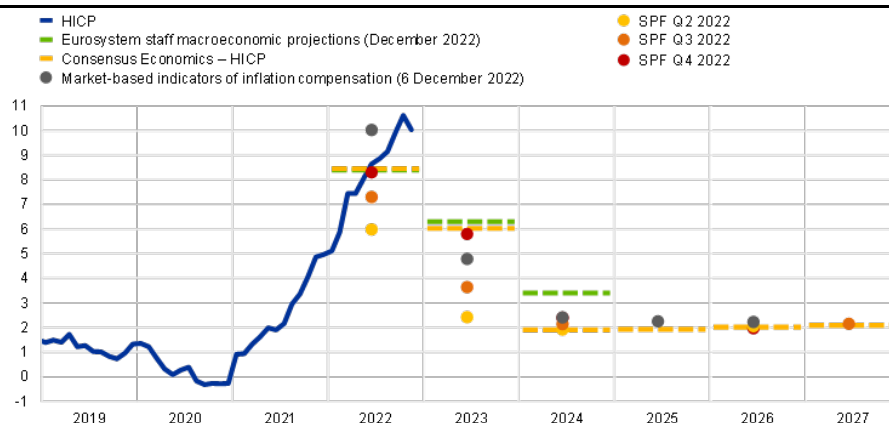
European markets were muted while waiting for the US December inflation release. Equity markets were slightly up throughout the region, with the Stoxx Europe 600 up 0.6%. The euro was broadly unchanged. **Euro area bond yields plunged, especially Italian yields, on a combination of factors.** Since yesterday's open, 10-year Italian yields fell 23 bps to 3.96%, and 10-year bunds yields fell 14 bps (to 2.16%). **The 10-year Italian spread to bunds traded at 180 bps, its lowest level since late April.** This happened against the backdrop of the global bond rally following investors' expectations for lower inflation

and a slower pace of tightening in Europe and the US going forward. Indeed, market expectations for the ECB terminal rate fell 11 bps to 3.3% in July yesterday, but have now retraced somewhat to 3.34%. The rally accelerated yesterday afternoon however after Bloomberg reported that German chancellor Olaf Scholtz will call for the European Union to create new joint financing instruments to counter the US's green plan.



ECB consumer expectations for inflation showed that inflation expectations eased in November for the first time since May, but remain significantly above the ECB's 2% target (blue line in chart below). Inflation expectations for the next 12 months declined to 5% in November, down from 5.4% the previous month. Expectations for inflation in 3 years also eased slightly to 2.9% from 3%.

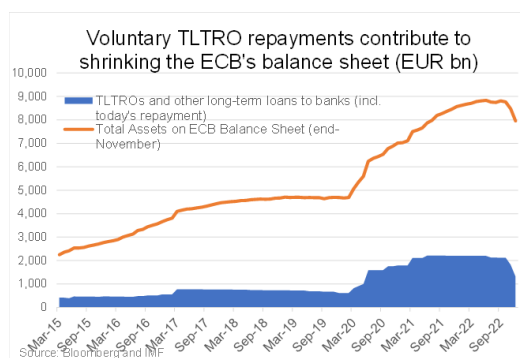
ECB Survey-based indicators of inflation expectations and market-based indicators of inflation compensation (annual percentage changes)



Source: ECB Economic Bulletin January 2023)

ECB officials continued to disseminate a hawkish message. Yesterday, Finish governor Rehn said that policy rates will still have to rise significantly to reach levels that are significantly restrictive to ensure a return to 2% medium-term inflation target. This will help dampen demand and also guard against persistent upward shift in inflation expectations. These comments were echoed almost word for word by Spanish governor De Cos later in the day.

A Bloomberg survey indicated that markets expect Eurozone banks to make about € 213 bn of TLTROs early repayments (median estimate), in the third iteration of these repayments. The ECB will announce the number tomorrow. Estimates for early repayments diverge widely, and range from €70 to 450 bn. Banks have already repaid about €700 bn early in November and December.



Sweden

The Swedish Riksbank reported a preliminary loss of SEK 81 bn (\$7.7 bn) for 2022 as rising market interest rates globally have reduced the value of assets on its balance sheet. Its capital is now at SEK 34 bn, below the 60 billion-krona level it considers a target level. Losses in coming years can be about SEK 70 bn to 100 bn, the central bank said, citing various scenarios it had prepared but excluding the most unlikely ones. According to the provisions on capital in the new Sveriges Riksbank Act, which applies from this year, the Riksbank shall submit a petition to the parliament to restore its equity if it falls too low. Some investors think that such losses could damage the Riksbank's credibility. Losses on assets acquired during years of QE is an issue in several central banks, with the Swiss National Bank posting a loss earlier this week and the UK's BOE in September.

Japan

The Bank of Japan (BOJ) reportedly may consider further tweaks to its monetary policy at the next policy meeting. According to news, the BOJ will review side effects of its monetary policy meeting and may consider adjusting its bond-buying as well as further policy tweaks in necessary. The Japanese yen appreciated (+0.5%), while long-end JGB yields rose (10-year: +0.5 bps; 30-year: +2.7 bps), with the 10-year JGB yield touching 0.504%. Meanwhile, 10-year JGB futures fell to a 9-year low. Today, the BOJ's fixed-rate bond purchases amounted to 2.81 tn yen (\$21.3 bn), a new record high, as yields breached the yield curve control limit. A rise in interest rates in Japan also led Japanese life insurers to sell a record amount of foreign bonds last month. Life insurers offloaded 2.25 tn yen (\$17.1 bn) of foreign bonds in December, bringing their total sales to an all-time high of 11.5 tn yen (\$87.2 bn) for whole year of 2022. Japanese equities gained (TOPIX: +0.4%; NIKKEI: flat).



Emerging Markets

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Most Asian equities gained, led by the Philippines (+1.9%), Indonesia (+0.7%), and Hong Kong SAR (+0.4%). **Asian currencies were mixed**. The Philippine peso (-0.9%) and Thai baht (-0.3%) depreciated, while Indonesian rupiah appreciated (+1.0%). **Long-end government bond yields generally declined**, with 10-year yields falling in Indonesia (-6.0 bps). In the **Philippines**, the central bank governor said that the monetary tightening cycle is approaching the end as the worse for price shocks was over. In **EMEA**, **equities rallied ahead of the release of US inflation, with currencies mixed**. The ruble (+1.8%) outperformed as oil prices rose further (up 1.4%, up 6% in past 5 days) with reports of substantial crude buying by China. **The Egyptian pound (-0.6% to 29.9 per U.S. dollar) traded lower** after yesterday's large devaluation albeit firmer than yesterday's intraday low of 32. **LATAM markets performance was positive yesterday**: equities markets were up, most currencies appreciated against the US dollar, and 5-year CDS spreads narrowed. **Peru's** central bank is expected to increase its benchmark interest rate by 25 basis points to 7.75% later today. **S&P Global raised its long-term local currency sovereign credit rating for Argentina** to CCC-/C from SD/SD and affirmed its foreign currency rating at CCC+/C after Argentina completed its peso-debt exchange last week. **Moody's outlook** for Latin American and Caribbean sovereign creditworthiness in 2023 is negative based on the region's weak economic growth, high borrowing costs, and persistent inflation pressures. High borrowing costs are likely to undermine debt repayment capacity, especially for lower-rated Latin American sovereigns.

EM Issuance Outlook

Analysts expect a sharp increase in the sale of US dollar denominated bonds (eurobonds) from emerging markets this year, even if issuance costs are relatively high versus history. Last year, sales of euro- and dollar-denominated debt by sovereign and corporate issuers from emerging markets fell 55% to \$321 bn, the lowest since 2011. JP Morgan expects that corporate debt issuance will climb almost 50% to \$300 bn this year, with another \$90 bn by sovereign issuers. **Morgan Stanley expects 2023 gross sovereign issuance to increase to \$143 bn**. This would imply an increase in net issuance by \$52 bn to \$78 bn. **Expectations are that Saudi Arabia, Turkey, Indonesia, Romania, and Hungary will be the largest issuers**. Yesterday, Turkey sold \$2.75 bn of 10-year eurobonds at a reported yield of 9.75%, below the initial yield guidance of 10.125%. Demand for the notes was perceived as sizable at around three times the size of the deal.

Slow Market

EM eurobond sales slumped 55% last year amid high cost of borrowing

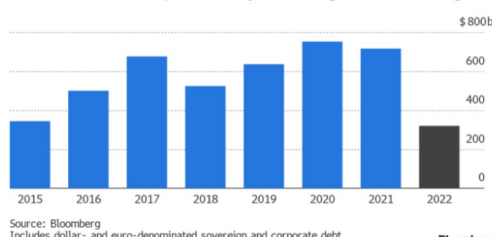
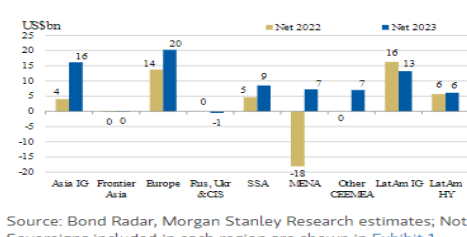
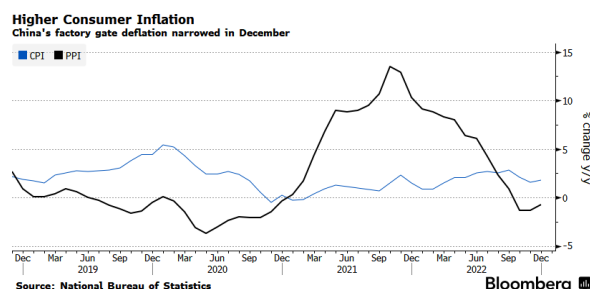


Exhibit 8: EM sovereign credit net issuance by region



China

Inflation remained subdued in December. CPI inflation edged up to 1.8% y/y in December from 1.6% in November on a sequential increase of food prices, in line with expectations. Meanwhile, PPI deflation continued for a third consecutive month as PPI declined 0.7% y/y (consensus: -0.1%). Analysts noted that the soft inflation data pointed to near-term weak economic activity amid ongoing COVID-19 outbreaks across the country; though, they expected that inflation will pick up following the reopening in China. The RMB appreciated (+0.1%). Chinese equities gained (CSI 300: +0.2%).



Mexico






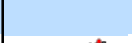



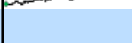



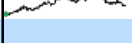











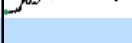

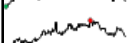
Mexico's peso appreciated as much as 0.7% to 18.93 per US dollar, breaching an important threshold for the first time since February 2020. The central bank's aggressive monetary policy stance of rising rates in lockstep with the US, relatively stable politics compared to peers, and nearshoring is providing a supportive backdrop for the currency, according to analysts at Wells Fargo Securities.



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Global Financial Indicators

1/12/23 8:01 AM	Level		Change				YTD	Since 23-Feb-22
	Last 12m	Latest	1 Day	7 Days	30 Days	12 M		
Equities			%				%	%
United States		3973	1.3	4	0	-16	3	-6
Europe		4133	0.8	4	5	-4	9	4
Japan		26450	0.0	3	-5	-7	1	0
China		4018	0.2	1	2	-16	4	-13
Asia Ex Japan		70	0.3	3	5	-18	8	-12
Emerging Markets		41	0.4	4	5	-20	8	-14
Interest Rates			basis points					
US 10y Yield		3.51	-3.1	-21	-10	177	-37	152
Germany 10y Yield		2.15	-5.3	-17	21	221	-42	192
Japan 10y Yield		0.51	0.5	8	26	38	9	31
UK 10y Yield		3.33	-8.3	-23	13	219	-35	185
Credit Spreads			basis points					
US Investment Grade		154	-3.0	-6	0	40	-4	12
US High Yield		447	-5.7	-24	-15	103	-33	41
Europe IG		79	-1.3	-8	-10	29	-12	7
Europe HY		411	-3.4	-38	-53	162	-63	60
Exchange Rates			%					
USD/Majors		103.07	-0.1	-2	-2	9	0	7
EUR/USD		1.08	0.1	2	2	-6	1	-5
USD/JPY		130.7	-1.3	-2	-5	14	0	14
EM/USD		51.0	0.1	2	2	-4	2	-4
Commodities			%					
Brent Crude Oil (\$/barrel)		83.9	1.5	7	7	9	-2	-1
Industrials Metals (index)		169	-0.6	5	1	-6	2	-10
Agriculture (index)		67	0.5	0	1	7	-3	-5
Implied Volatility			%					
VIX Index (% change in pp)		21.5	0.4	-1.0	-3.5	3.9	-0.2	-9.5
US 10y Swaption Volatility		117.7	0.1	-8.9	-26.9	38.2	-8.0	23.4
Global FX Volatility		10.5	0.0	-0.3	0.3	3.4	-0.2	3.0
EA Sovereign Spreads			10-Year spread vs. Germany (bps)					
Greece		192	-5.1	-22	-13	31	-13	-48
Italy		180	-2.8	-21	-9	48	-34	9
Portugal		89	-1.0	-10	-3	27	-12	-3
Spain		97	-1.4	-9	-6	28	-12	-6

Colors denote **tightening**/**easing** financial conditions for observations greater than ± 1.5 standard deviations.

Data source: Bloomberg.

Emerging Market Financial Indicators

Last updated: 1/12/2023 8:06 AM	Exchange Rates							Local Currency Bond Yields (GBI EM)								
	Level		Change (in %)				YTD	Since 23-Feb-22	Level		Change (in basis points)				YTD	Since 23-Feb-22
	Last 12m	Latest	1 Day	7 Days	30 Days	12 M			Last 12m	Latest	1 Day	7 Days	30 Days	12 M		
	vs. USD		(+) = EM appreciation						% p.a.							
China		6.75	0.2	1.9	3	-6	2	-6		3.1	1.5	9	-2	28	7	28
Indonesia		15339	0.9	1.8	2	-7	2	-7		6.8	-5.6	-24	-20	34	-19	26
India		82	0.0	1.2	1	-9	1	-9		7.4	3.8	2	14	63.1	-6	
Philippines		55	-0.9	0.8	1	-7	1	-8		6.1	0.0	0	5	155	5	108
Thailand		33	0.4	2.2	5	0	4	-3		2.6	-0.5	-5	4	49	-8	33
Malaysia		4.36	0.3	0.7	1	-4	1	-4		4.0	1.3	-4	-12	33	-7	30
Argentina		181	-0.2	-1.1	-5	-43	-2	-41		83.8	-29.1	-236	-519	3480	-444	3581
Brazil		5.15	0.3	3.9	3	7	3	-3		12.3	-5.5	-67	-76	103	-26	80
Chile		821	0.3	3.9	6	0	4	-4		5.0	-2.5	-33	-28	-93	-37	-95
Colombia		4701	0.7	5.6	3	-15	3	-17		9.7	0.0	-55	-36	253	-8	182
Mexico		18.92	0.0	2.1	5	8	3	7		8.1	0.0	-30	-24	50	-59	30
Peru		3.8	0.2	1.2	1	3	1	-1		7.8	0.4	-22	3	172	-21	176
Uruguay		40	0.0	0.3	-2	12	0	7		10.7	0.0	0	-16	202	0	253
Hungary		371	-0.3	1.4	6	-17	1	-14		7.7	-22.0	-87	-167	305	-192	287
Poland		4.36	0.0	2.2	2	-9	0	-7		5.2	-5.5	-23	-37	136	-100	125
Romania		4.6	0.0	2.0	2	-6	1	-5		7.3	-16.6	-25	-21	220	-43	210
Russia		67.9	1.7	7.0	-7	10	9	20		11.7	0.0	88	92	249	-21	47
South Africa		16.9	0.3	1.8	4	-9	1	-10		8.6	-2.0	-36	-63	98	-54	104
Turkey		18.78	0.0	-0.1	-1	-29	0	-26		9.8	32.0	126	-116	-1451	0	-1259
US (DXY; 5y UST)		103	-0.1	-1.9	-2	9	0	7		3.64	-2.3	-28	-15	212	-37	173

	Equity Markets								Bond Spreads on USD Debt (EMBIG)							
	Level		Change (in %)				YTD	Since 23-Feb-22	Level		Change (in basis points)			YTD	Since 23-Feb-22	
	Last 12m	Latest	1 Day	7 Days	30 Days	12 M			Last 12m	Latest	7 Days	30 Days	12 M			
								basis points								
China		4018	0.2	1	2	-16	4	-13		185	3	3	-11	8	-23	
Indonesia		6630	0.7	0	-3	0	-3	-4		172	8	18	6	32	-13	
India		59958	-0.2	-1	-4	-2	-1	5		155	11	14	31	13	1	
Philippines		6834	1.9	1	4	-6	4	-7		145	17	24	44	48	8	
Thailand		1687	0.1	1	4	0	1	-1		0	0	0	0	0	0	
Malaysia		1489	0.1	1	1	-5	0	-6		107	3	13	-8	7	-26	
Argentina		224628	4.1	12	35	164	11	146		2017	-81	-337	206	-188	280	
Brazil		112517	1.5	5	7	6	3	0		279	-2	20	-40	5	-52	
Chile		5171	0.7	1	-2	15	-2	18		154	6	18	9	22	-20	
Colombia		1343	0.6	4	9	-7	4	-11		383	13	1	36	11	-9	
Mexico		53209	1.7	6	5	-1	10	4		377	-10	0	39	-4	7	
Peru		22568	-0.8	4	4	-4	6	-4		198	3	33	36	18	8	
Hungary		46138	-0.3	2	5	-15	5	-3		250	-4	31	129	28	97	
Poland		62093	1.3	4	10	-15	8	-1		106	25	28	84	33	90	
Romania		12394	0.5	2	2	-8	6	-6		276	-6	24	83	20	43	
Russia		2187	0.0	1	1	-43	2	-29		3411	-577	938	3228	3234	2897	
South Africa		79023	0.6	5	6	4	8	5		353	-13	-31	1	-14	-36	
Turkey		4826	2.1	-6	-7	134	-12	139		493	44	51	-95	53	-70	
Ukraine		514	0.0	-1	-1	-2	-1	-1		4176	61	225	3390	97	2703	
EM total		41	-0.2	4	5	-20	8	-14		388	4	12	-14	12	-70	

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

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