



Global Markets Monitor

Monetary and Capital Markets Department
Global Markets Analysis Division

Tuesday, January 22, 2019

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- **US equities post strong gains last week on news of improving US-China relations ([link](#))**
- **UK PM May rejects idea of second referendum; looks to continue discussions with EU ([link](#))**
- **ECB bank lending survey signals more cautious standards on corporate loans ([link](#))**
- **Fund managers favored exposures to Brazil and Mexico at the end of 2018 ([link](#))**
- **Chinese GDP growth slows in Q4 but consumer and industrial activity stabilizes ([link](#))**

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Global equity market rally stalls as growth and political worries persist

Risk assets are trading lower as focus remains on the state of global growth, Brexit, and trade tensions. To start the week, investors focused on a mixed batch of data from China and the newly proposed plan of action for Brexit by the UK's PM May. Although China's GDP growth slowed in Q4, the results were inline with forecasts and were offset by a stabilization in consumer and industrial activity. Asian equities initially traded higher as investors viewed the data as suggesting Chinese growth could be finding a bottom, but pulled back overnight on renewed pessimism over US-China trade relations. In the UK, PM May maintained her position that she will not back a second referendum, and will pursue a compromise with EU leaders and MPs. While US equity and bond markets were closed yesterday, they ended last week on a strong note with equities rallying over 1% and Treasury yields up 2 to 5 bps across the curve. The catalyst for the move appeared to be tied to further improvement in US-China trade relations, but S&P 500 futures and Treasury yields are lower this morning amid news of a lack of progress in US-China talks on non-tariff barriers. The BoJ and ECB hold policy meetings later this week where the attention will be on communication around the economic outlook, as no change in policy stance is expected.

Key Global Financial Indicators

Last updated: 1/22/19 8:12 AM	Level		Change from Market Close				
	Last 12m	Latest	1 Day	7 Days	30 Days	12 M	YTD
Equities			%				%
S&P 500		2671	0.0	3	11	-5	7
Eurostoxx 50		3109	-0.5	1	4	-15	4
Nikkei 225		20623	-0.5	0	2	-13	3
MSCI EM		42	-0.6	2	8	-18	6
Yields and Spreads			bps				
US 10y Yield		2.76	0.0	4	-3	11	7
Germany 10y Yield		0.24	-1.4	4	-1	-33	0
EMBIG Sovereign Spread		372	-3	-17	-31	104	-42
FX / Commodities / Volatility			%				
EM FX vs. USD, (+) = appreciation		63.2	0.0	0	2	-11	1
Dollar index, (+) = \$ appreciation		96.4	0.1	0	-1	0	0
Brent Crude Oil (\$/barrel)		61.8	-1.5	2	15	-11	15
VIX Index (% change in pp)		18.6	0.8	0	-12	7	-7

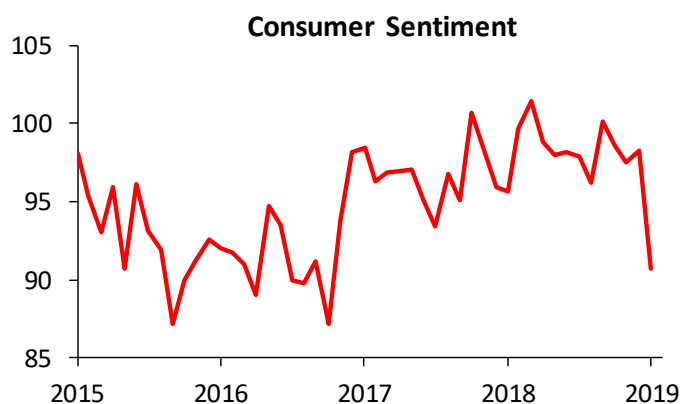
Colors denote **tightening/easing** financial conditions for observations greater than ± 1.5 standard deviations. Data source: Bloomberg.

Central bank policy meetings for the ECB, BoJ and Bank of Korea highlight a week where world leaders are also convening at Davos. Solid earnings releases by US firms should continue apace, but China trade tensions and the partial government shutdown will continue to cloud market sentiment. The shutdown could likely delay the release of a raft of home data reports throughout the week and durable goods out Friday. Manufacturing activity as measured by PMIs are due out in a number of major economies Thursday, and Germany releases its seminal ZEW report (Tuesday) and Ifo report (Friday).

United States

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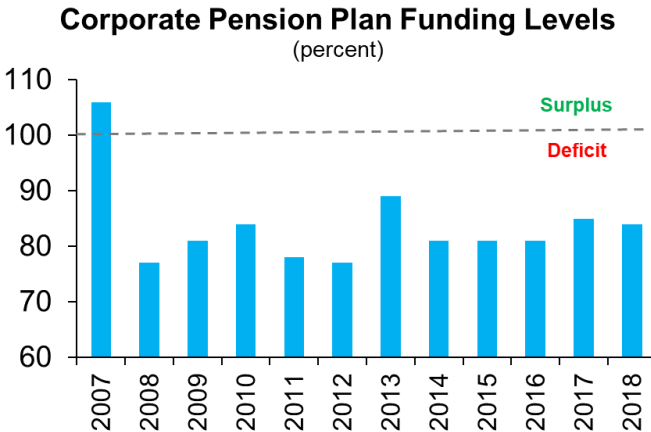
US markets were closed Monday for a national holiday. **Stock prices rallied Friday, with major indices posting gains of 1-1.4% on news that the US and China may be closer to a trade deal.** The risk-on sentiment helped push up Treasury yields, with the 2-year yield climbing 5 bps to 2.61% and the 10-year 4 bps to 2.79%. Markets are pricing in about a 30% chance of an FOMC rate hike by the end of the year. Contacts were also focused on a fall in consumer sentiment reported by the University of Michigan on Friday. The December drop in the headline index was the steepest since late 2012. Analysts ascribed the severity of the fall primarily to the ongoing government shutdown, but also added that the December stock market plunge played a role. Nonetheless, market participants remain divided on the knock-on effects of the government shutdown. **This morning, S&P 500 futures point to a 0.6% decline at the open and the benchmark 10-year US Treasury yield is down about 4 bps to 2.75%, in line with the general risk-off sentiment to start the week.**



Source: Bloomberg

Shares of Fannie Mae (+33.9%) and Freddie Mac (+31.5%) surged Friday after the acting head of the Federal Housing Finance Agency commented the administration is working on a proposal to release the mortgage finance giants from government control, possibly bypassing Congress. The two firms have been under government conservatorship since September 2008.

Corporate pension plans registered an aggregate funding level of 84% at end-2018, down slightly from the 85% of a year earlier according to Willis Towers Watson. Plans benefitted from rising equity markets, higher bond yields, and solid contributions from plan sponsors through most of the year, with the advisory firm noting that funding levels topped 90% at the end of Q3—with similar findings by Wilshire Consulting and Mercer. But the equity losses in Q4 (and particularly in December) erased the gains for the year. December in fact was the worst month for pension funds in a decade. Public sector pension funds have generally lower funding level ratios than their private sector counterparts, and Bloomberg gauges that the December market plunge saw the value of their assets fall by about 7%. Flow of Funds data indicate the total financial assets of private (defined benefit and defined contribution) pension funds stood at \$10.0 tn at the end of Q3, with another \$9.0 tn in state and local government pensions, and \$4.0 tn in federal pensions.



Source: Willis Towers Watson

Europe

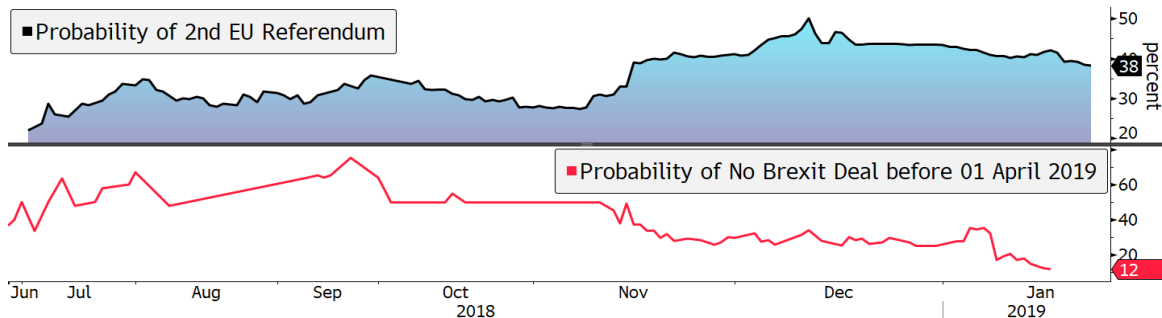
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European stocks drifted 0.3% lower this morning following the IMF's growth downgrade for some countries: EuroStoxx 600 (-0.2%), DAX (-0.3%), and CAC 40 (-0.4%). **Bank equities (-1.3%) underperformed notably**, dragged down by UBS (-4.1%) on disappointing 2018Q4 results, and Deutsche Bank (-3.2%) after the announcement of a €12 bn-lawsuit by businessman Mr. Sabet over a 2013 property transaction.

Euro area sovereign bond markets held steady. German 10-year bunds are flat at 0.25%, while Italian and Spanish bonds inched down 2 bps to 2.73% and 1.35%, respectively. Portuguese bonds are at 1.73% (-1 bp). Demand for Italian, Spanish, and Portuguese bonds has remained strong in recent auctions, with cover ratios ranging from 3.6 to 6.

Labour leader Jeremy Corbyn has tabled a proposal that would allow MPs to vote on their preferred measure to break the current deadlock over Brexit. Although a customs union with the EU remains the preferred option for Labour's leadership, the proposed options could pave the way for a second Brexit referendum. Most analysts expect Corbyn's proposals to be rejected by parliament. **PM May has again rejected the idea of a second referendum**, arguing it would undermine trust in democracy and threaten the UK's social cohesion. Separately, **the EU's chief negotiator Mr. Barnier has reiterated that the existing offer for a Brexit agreement is the best possible deal for Britain.** The European Commission, in turn, has warned the EU27 finance ministers to step-up plans for a no-deal Brexit.

Odds of a 2nd EU Referendum

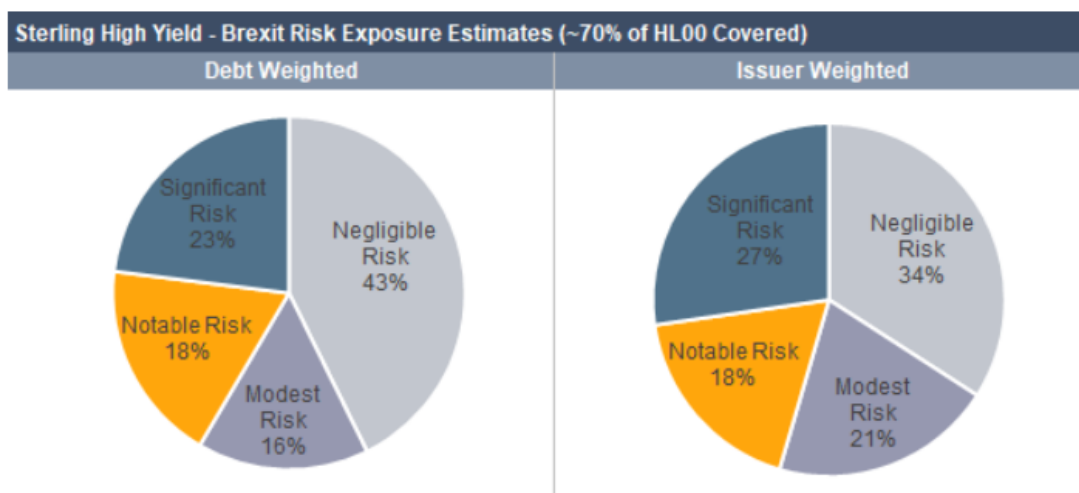


Source: Average Odds from Oddschecker
 ODCHEUN Index (Avg Implied Probability of 2nd EU Referendum - NO) Brexit 2nd Re

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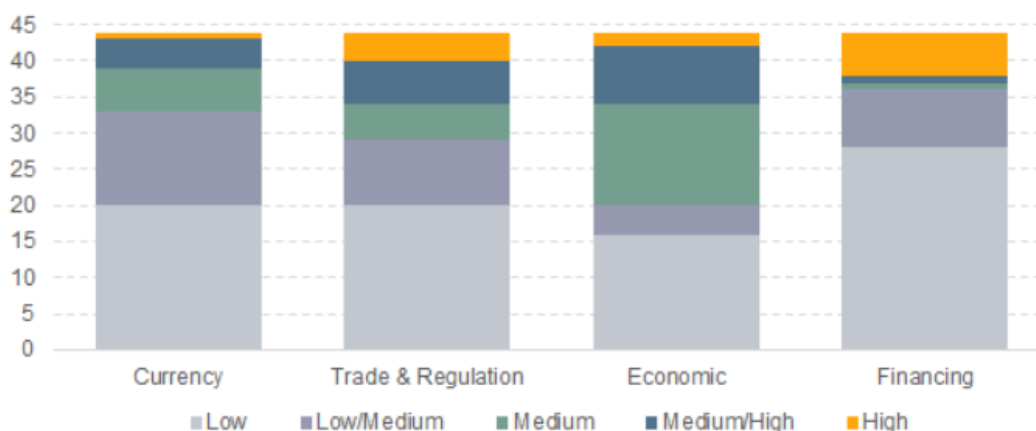
Research by CreditSights finds that **around 40% of sterling high-yield issuers could be at notable or significant risk due to Brexit**. By sector, autos, building materials and construction, and food and restaurants have the highest risk exposures. In terms of drivers, the largest vulnerability stems from risks to the availability of funding (refinancing and working capital management), followed by the risk of changes to existing trade and regulation regimes.



Source: CreditSights, BofAML





































































Note: This breaks issuers down by their single highest score on our matrix, i.e. if an issuer has any buckets that qualify as high, it has Significant Risk; if an issuer's highest bucket is medium/high, it qualifies as Notable Risk; if an issuer's highest allocation is Medium it qualifies as Modest Risk; if an issuer only scores medium/low or low across all buckets, it qualifies as Negligible Risk.

Brexit Risk Exposure Estimates: Degree of Risk, Weighted by Issuer



Source: CreditSights

The latest ECB Bank Lending Survey (BLS) suggests credit underwriting is turning more cautious in the Eurozone. The 2018Q4 BLS suggested greater bank loan underwriting. Despite continued support from low interest rates, evidence of credit demand was mixed. Banks reporting stronger consumer credit demand fell from 22% to 8%, and those reporting stronger corporate demand fell from 12% to 8%. In addition, banks' credit underwriting standards are tightening on the 'second derivative', in the sense that a declining proportion of reporting banks are reporting net easing of standards. Actual lending still appears to be solid, with 4Q18 corporate and overall private sector credit growth at +4.0% and +3.6% yoy, respectively.

	Enterprises						House Purchase						Consumer credit					
	Credit standards			Demand			Credit standards			Demand			Credit standards			Demand		
	Q4	change vs Q3	expected change in Q1	Q4	change vs Q3	expected change in Q1	Q4	change vs Q3	expected change in Q1	Q4	change vs Q3	expected change in Q1	Q4	change vs Q3	expected change in Q1	Q4	change vs Q3	expected change in Q1
Euro area	-1			9			-1			12			2			8		
Germany	-3			22			0			10			0			10		
Spain	0			-20			0			-11			10			0		
France	0			-15			-2			12			0			9		
Italy	10			20			10			10			0			0		
Netherlands	-26			28			-35			52			0			17		

Source: ECB, UBS. Note: **Credit standards:** A positive net percentage balance indicates a larger proportion of banks have tightened credit standards (net tightening). A negative number indicates a net easing of credit standards. **Loan demand:** A positive net percentage balance indicates an increase in loan demand, whereas a negative figure would indicate a decline in loan demand. **Colour code:** Green: improvement; red: worsening; yellow: unchanged.

European Data releases:

- The January **German ZEW survey** of Expectations came in slightly better than expected at -15.0, compared to -18.5 expected and -17.5 last month. However, the Current Economic Situation survey disappointed at 27.6, vs. 43.0 expected.
- The **UK's unemployment rate** fell to 4.0% in November, the lowest level since 1976.

Other Mature Markets [back to top](#)

Japan

The Nikkei declined slightly over the last two sessions, in line with the moves in global markets. The index is still up 3.0% for the year. **The 10-year yield continues its recent decline and is now back to near zero**, down from 0.03% earlier in the month and recent high of 0.16% in October 2018. The yen is slightly strong against the dollar at ¥109.4, around where it started the year.

Emerging Markets

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Key Emerging Market Financial Indicators

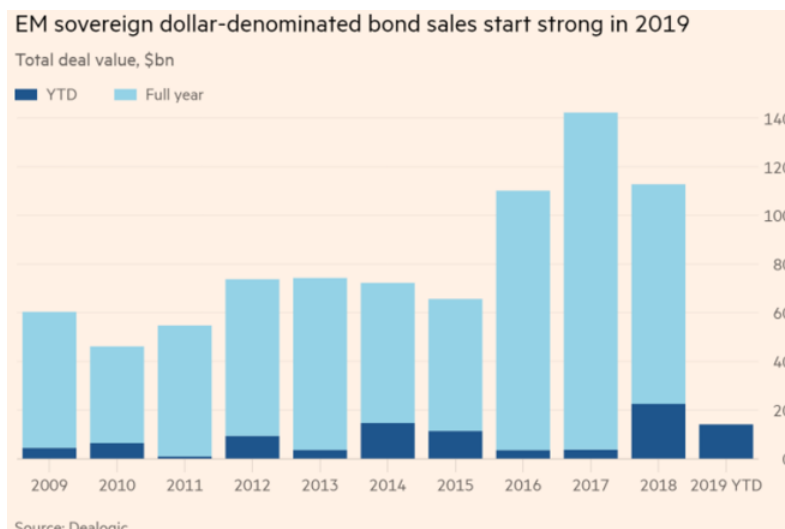
Last updated: 1/22/19 8:16 AM	Level		Change				YTD
	Last 12m	index	1 Day	7 Days	30 Days	12 M	
Major EM Benchmarks			%				%
MSCI EM Equities		41.55	-0.6	2	8	-18	6
MSCI Frontier Equities		27.90	0.2	1	7	-23	7
EMBIG Sovereign Spread (in bps)		372	-3	-17	-31	104	-42
EM FX vs. USD		63.17	0.0	0	2	-11	1
Major EM FX vs. USD			%, (+) = EM currency appreciation				
China Renminbi		6.81	-0.1	-1	1	-6	1
Indonesian Rupiah		14220	0.1	-1	2	-6	1
Indian Rupee		71.44	-0.2	-1	-2	-11	-2
Argentine Peso		37.79	-0.2	-2	1	-49	0
Brazil Real		3.75	0.1	-1	4	-15	3
Mexican Peso		19.18	-0.1	-1	4	-3	2
Russian Ruble		66.45	-0.1	1	3	-15	5
South African Rand		13.90	-0.5	-1	5	-13	3
Turkish Lira		5.35	-0.5	2	-1	-29	-1
EM FX volatility		9.17	0.0	-0.2	-0.4	1.2	-0.6

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

EM assets traded poorly on Monday amid thin liquidity due to the US holiday and growing concerns about US-China trade negotiations. According to Bloomberg, US and China have made little progress on intellectual property rights, raising doubts about a trade deal. In **Latin America**, the Brazilian real fell marginally against the dollar, depreciating for a fifth day in a row, the longest losing streak in six weeks. Markets remain in wait and see mode as President Bolsonaro is still considering "several proposals" for the pension reform bill as he travels to Davos this week. In **Asia**, equity markets were mostly lower, led by a 1.2% decline in the Shanghai Comp. Regional currencies depreciated against the dollar, notably the Malaysian ringgit and Philippine peso (both around 0.4% weaker). In **EMEA**, equity markets are broadly but modestly lower, with Turkey (+1.2%) being the notable exception. Currencies are mixed, with the South African rand and the Turkish lira depreciating 0.6%, and the Ukrainian Hryvnia appreciating 0.5%.

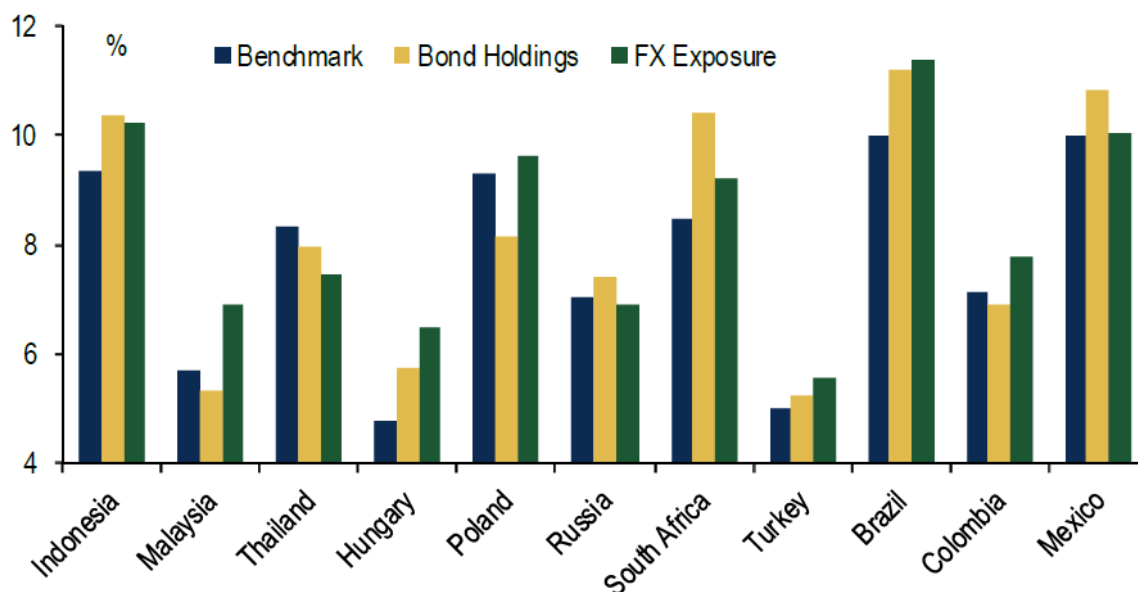
EM Sovereign Debt Issuance

After a 20% drop in value in 2018, EM sovereign dollar issuance started strong in 2019. Up until January 17, issuance was \$14bn, the third best on record as issuers took advantage of the decline in market expectations of further rate hikes by the Federal Reserve. Last week Mexico (2029) raised \$2bn and Uruguay (2031) \$850mn. Earlier in the year key issues included two bonds by Saudi Arabia (2050 and 2029) for a total of \$7.5bn and one bond by Turkey (2029) for \$2bn.



According to BAML analysts, in December 2018, Mexican and Brazilian bonds saw the biggest increases in fund manager exposures while overweight exposures to Indonesia, South Africa and Russia were trimmed back. Relative to the benchmark, South African and Brazilian bonds enjoy the highest overweight exposures. On the other hand, funds increased their underweight positions in Poland, Malaysia and Colombia.

Chart of the day - Brazil favorite amongst the real money investors in Dec



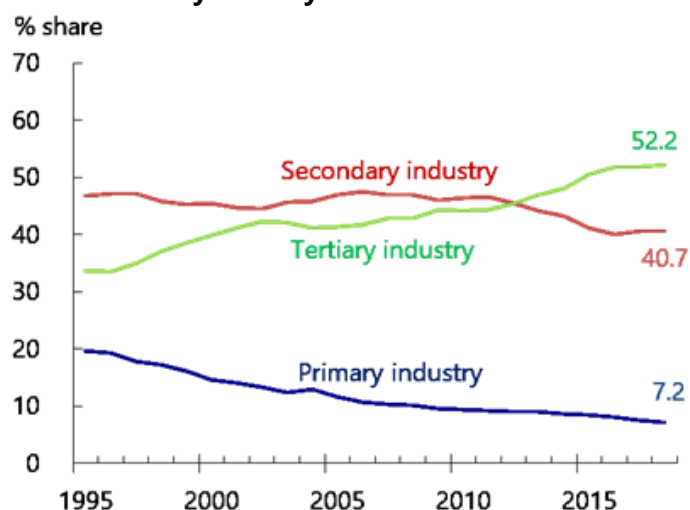
Source: BofA Merrill Lynch Global Research, Fund factsheets

China

GDP growth declined to 6.4% yoy in Q4 from 6.5% yoy in Q3 last year. Investment growth slowed, while industrial production rebounded and retail sales steadied. On the whole, analysts note growth momentum seems to be stable but with some signs of slowing. Meanwhile, the Chinese authorities are likely to lower growth target from around 6.5% last year to 6 – 6.5% this year.

Slower growth is expected to weigh on inflows into risky assets. Market data show that assets under management at domestic equity mutual funds shrank 12% in Q4 last year from a year ago to RMB194 billion (US\$28.6 billion), while fixed income funds expanded 20% to RMB3 trillion. This may partly explain the falling government bond yields over the same period. Another positive factor for fixed income assets is the inclusion of Chinese government and policy bank bonds in various global bond indices, which is expected to boost the demand from offshore investors. According to estimates by Standard Chartered, passive inflows into China's bond market following wider inclusion could reach US\$50 billion this year. While the moderation of GDP growth may be negative for investment sentiment, a bright spot is that economic rebalancing is in progress. Contribution from final consumption to GDP growth picked up to 76% in 2018 from 58% in 2017. The importance of the service sector is also growing, with its share in GDP rising to 52.2% from 51.9% over the same period.

China's GDP by industry



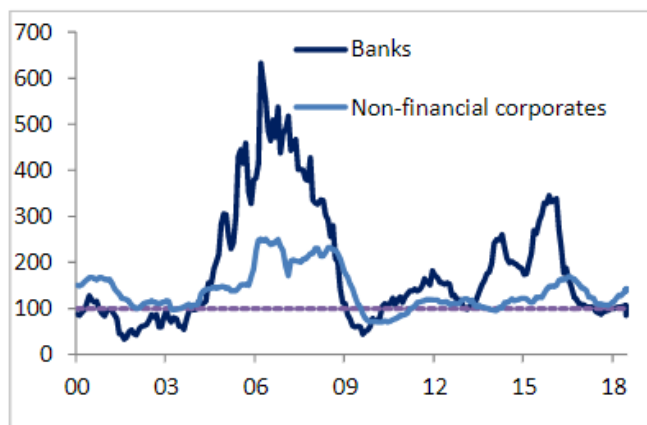
Sources: NBS, CEIC.

Worries about dimmer global growth prospects and US-China trade tensions exerted downward pressure on the Chinese equity market, while the renminbi weakened following a stronger US dollar against regional currencies. IMF cut its global growth forecast for 2019 by 0.2 percentage point to 3.5% in its latest projection, citing significant higher risk stemming from US-China trade tensions and weaker economic performance in key European economies. The Shanghai Composite and Shenzhen small-cap ChiNext slipped 1.2% and 1.8% respectively. In the currency market, the renminbi weakened by 0.3% against US dollar in the onshore market and depreciated by 0.2% in the offshore market.

Turkey

The deleveraging of the financial system continues, and banks' external debt rollover ratio has been declining, now at an estimated 85%. Analysts at BAML expect this trend to continue, with rollover ratios falling in 2019 as international banks reduce their exposure further and economic activity decelerates. This process has led to a reduction in external debt stock of about \$15 bn. Debt due from banks and corporates amounts to about \$35 bn for the first half of 2019.

Chart 1: Banks' long-term external debt rollovers are declining (%)


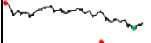









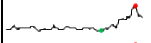
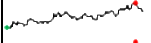










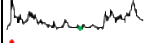







Source: CBT, Haver, BofA Merrill Lynch Global Research

List of GMM Contributors (Global Markets Analysis Division, MCM Department)
Anna Ilyina*Division Chief***Peter Breuer***Deputy Division Chief***Will Kerry***Deputy Division Chief***Sergei Antoshin***Senior Economist***John Caparusso***Senior Financial Sector Expert***Sally Chen***Senior Economist***Fabio Cortés***Senior Economist***Mohamed Jaber***Senior Financial Sector Expert***David Jones***Senior Financial Sector Expert***Sanjay Hazarika***Senior Financial Sector Expert***Rebecca McCaughrin***Senior Financial Sector Expert***Juan Solé***Senior Economist***Jeffrey Williams***Senior Financial Sector Expert***Akihiko Yokoyama***Senior Financial Sector Expert***Dimitrios Drakopoulos***Financial Sector Expert***Tryggvi Gudmundsson***Economist***Henry Hoyle***Financial Sector Expert***Robin Koepke***Economist***Thomas Piontek***Financial Sector Expert***Jochen Schmittmann***Economist***Ilan Solot***Financial Sector Expert***Nour Tawk***Economist***Martin Edmonds***Senior Data Mgt Officer***Yingyuan Chen***Senior Research Officer***Rohit Goel***Research Officer***Piyusha Khot***Research Assistant***Xingmi Zheng***Research Assistant*

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Global Financial Indicators

Last updated: 1/22/19 8:13 AM	Level		Change				YTD
	Last 12m	Latest	1 Day	7 Days	30 Days	12 M	
Equities			%				%
United States		2671	0.0	3	11	-5	7
Europe		3108	-0.5	1	4	-15	4
Japan		20623	-0.5	0	2	-13	3
China		2580	-1.2	0	3	-26	3
Asia Ex Japan		67	0.6	2	7	-18	5
Emerging Markets		42	-0.6	2	8	-18	6
Interest Rates			basis points				
US 10y Yield		2.76	0.0	4	-3	11	7
Germany 10y Yield		0.24	-1.4	4	-1	-33	0
Japan 10y Yield		0.00	-0.5	-1	-4	-8	0
UK 10y Yield		1.32	-0.3	6	0	-4	4
Credit Spreads			basis points				
US Investment Grade		132	-4.4	-10	-5	47	-15
US High Yield		434	4.3	-18	-77	99	-87
Europe IG		77	1.7	-4	-15	33	-10
Europe HY		325	7.4	-10	-39	95	-27
EMBIG Sovereign Spread		372	-3.0	-17	-31	104	-42
Exchange Rates			%				
Dollar Index (DXY)		96.40	0.1	0	-1	7	0
USDEUR		1.14	-0.1	-1	0	-7	-1
USDJPY		109.4	0.2	-1	1	1	0
EM FX vs. USD		63.2	0.0	0	2	-11	1
Commodities			%				
Brent Crude Oil (\$/barrel)		62	-1.5	2	15	-10	15
Industrials Metals (index)		113	-0.6	3	2	-17	4
Agriculture (index)		43	0.0	1	2	-9	3
Implied Volatility			%				
VIX Index (% change in pp)		18.6	0.8	-0.5	-11.5	7.3	-6.8
10y Treasury Volatility Index		3.8	-0.2	-0.2	-1.1	-0.4	-0.7
Global FX Volatility		8.1	0.0	-0.3	-0.6	0.6	-0.9
EA Sovereign Spreads			10-Year spread vs. Germany (bps)				
Greece		390	-0.1	-16	-21	63	-25
Italy		250	-0.4	-17	-8	114	0
Portugal		148	-2.0	2	4	11	0
Spain		109	-1.6	-9	-6	27	-8

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: 1/22/2019 8:18 AM	Exchange Rates						YTD	Local Currency Bond Yields (GBI EM)						
	Level		Change (in %)					Level		Change (in basis points)				YTD
	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		6.81	-0.1	-0.7	1	-6	1		3.1	1.4	-2	-18	-94	-12
Indonesia		14220	0.1	-0.9	2	-6	1		8.3	0.2	4	12	188	13
India		71	-0.2	-0.6	-2	-11	-2		7.6	-0.2	12	18	2	13
Philippines		53	-0.3	-1.8	0	-4	-1		5.9	0.0	-17	-43	106	-43
Thailand		32	-0.1	0.3	2	0	2		2.7	-0.7	3	0	38	2
Malaysia		4.13	-0.5	-0.6	1	-5	0		4.0	0.0	-1	-7	9	-6
Argentina		38	-0.2	-1.8	1	-49	0		21.2	0.2	-60	-189	535	-180
Brazil		3.75	0.1	-0.9	4	-15	3		8.0	-2.4	-3	-17	-80	-13
Chile		673	-0.1	0.2	2	-10	3		4.5	0.0	4	1	-31	4
Colombia		3132	-0.3	0.3	5	-9	4		6.6	-0.5	4	2	27	4
Mexico		19.18	-0.1	-1.0	4	-3	2		8.7	2.5	10	-11	111	1
Peru		3.3	-0.2	0.5	1	-3	1		5.7	-0.1	-1	-6	86	-3
Uruguay		33	0.2	0.3	-1	-13	-1		10.3	0.0	-23	-60		-44
Hungary		280	-0.2	1.1	1	-10	0		2.2	4.5	17	-2	87	-1
Poland		3.77	0.0	-0.3	0	-10	-1		2.3	0.0	8	3	-37	2
Romania		4.2	-0.5	-1.5	-2	-9	-3		4.5	10.0	17	28	62	27
Russia		66.5	-0.1	0.8	3	-15	5		8.1	0.0	-8	-41	90	-35
South Africa		13.9	-0.5	-1.1	5	-13	3		9.6	0.9	13	-7	41	1
Turkey		5.35	-0.5	1.8	-1	-29	-1		16.5	-4.7	-14	-89	427	-33
US (DXY; 5y UST)		96	0.1	0.4	-1	7	0		2.59	-2.9	6	-4	15	8

	Equity Markets							Bond Spreads on USD Debt (EMBIG)							
	Level		Change (in %)					YTD	Level		Change (in basis points)				YTD
	Last 12m	Latest	1 Day	7 Days	30 Days	12 M	Last 12m		Latest	1 Day	7 Days	30 Days	12 M		
									basis points						
China		2580	-1.2	0	3	-26	3		184	1	-1	-8	38	-10	
Indonesia		6469	0.3	1	5	0	4		205	2	-7	-20	52	-31	
India		36445	-0.4	0	2	2	1		185	-1	-7	-4	80	-11	
Philippines		8009	0.0	0	7	-11	7		99	2	-7	-14	20	-22	
Malaysia		1702	1	2	2	-7	1		147	1	-6	-6	46	-15	
Argentina		35303	0.6	5	24	5	17		677	4	-18	-144	311	-138	
Brazil		95836	-0.1	2	12	17	9		245	2	-9	-24	22	-28	
Chile		5452	-0.4	1	8	-6	7		145	1	-4	-13	36	-21	
Colombia		1399	0.4	0	7	-10	6		196	2	-2	-28	40	-32	
Mexico		44029	-0.5	1	6	-12	6		315	3	-19	-34	79	-39	
Peru		19580	0	0	3	-7	1		151	3	-1	-10	31	-17	
Hungary		40863	-0.1	1	3	0	4		135	1	-3	-4	50	-13	
Poland		59650	-0.4	0	4	-11	3		62	0	-1	-12	18	-23	
Romania		7138	-0.3	1	3	-16	-3		213	0	4	3	101	-8	
Russia		2464	-0.2	1	5	7	4		215	-2	-10	-27	50	-37	
South Africa		54040	-0.2	1	5	-11	2		322	-3	-7	-30	98	-43	
Turkey		99027	1.1	6	8	-16	8		413	-12	-47	-2	131	-16	
Ukraine		557	0.1	0	0	68	0		663	-22	-68	-102	273	-124	
EM total		24	0.0	2	6	-13	6		372	-3	-17	-31	104	-42	

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