GLOBAL MARKETS ANALYSIS

Monetary and Capital Markets

Global Markets Monitor

FRIDAY, JANUARY 12, 2024

LEAD EDITOR: FABIO CORTES

- **US Treasury yields fall sharply after softer than expected PPI** (link)
- **US corporate bonds expected to outperform on favorable supply-demand dynamics** (link)
- **European government bond sales hit an all-time high this week** (link)
- **Bank of Japan officials considering cuts to their forecasts for growth and inflation** (link)
- **Disinflation narrative expected to drive returns for EM local currency bonds** (link)
- **Markets expect a cut in China's MLF rate next Monday** (link)
- **Peru's central bank delivers fifth consecutive 25 bps rate cut** (link)
- **Central Bank of Türkiye reportedly close to the end of its tightening cycle** (link)

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Markets cautious to end the week

US equity futures lacked direction and European bourses rose modestly amid rising geopolitical tensions in the Red Sea and a plethora of central bank speeches and interviews. In contrast to the CPI release yesterday, December PPI was lower than expected this morning, with Treasury yields falling sharply immediately following the release. Across the pond, euro area sovereign bond yields fell in a week that marks and an all-time high for sales of European government bonds. The last 24 hours saw a number of central bank speeches and interviews across both sides of the Atlantic. In the US, Fed Cleveland President Mester said that it was premature to consider cutting interest rates as soon as March, and Richmond President Barkin reiterated that he is looking for more evidence that inflation is headed towards the target. In the euro-area, president Largarde remarked that the ECB will start lowering interest rates once it is convinced that inflation is headed back to its 2% target, and Croatia's central bank governor Vujcic noted that markets continued to be overly optimistic about the timing of the first ECB rate cut. In commodities, oil prices jumped on reports of US and UK strikes against Houthi revels in Yemen. Elsewhere, Japanese equities continued their recent outperformance, gaining 1.5% this morning and reaching a new 34-year high amid a weak yen and prospects of a new tax-free retirement savings program. In emerging markets, the central bank of Peru delivered its fifth consecutive rate cut while markets expect a cut in China's medium-term lending facility (MLF) rate next Monday amid persistent deflationary pressures.

Key Global Financial Indicators

Last updated: 1/12/24 8:16 AM	Level		Change from Market Close				
	Last 12m	Latest	1 Day	7 Days	30 Days	12 M	YTD
Equities			%				%
S&P 500		4780	-0.1	2	3	20	0
Eurostoxx 50		4463	0.5	0	-2	8	-1
Nikkei 225		35577	1.5	7	8	36	6
MSCI EM		39	0.4	-1	0	-5	-3
Yields and Spreads			bps				
US 10y Yield		4.00	3.5	-4	-20	56	12
Germany 10y Yield		2.22	-1.9	6	-1	6	19
EMBIG Sovereign Spread		402	-1	-2	4	-61	18
FX / Commodities / Volatility			%				
EM FX vs. USD, (+) = appreciation		47.8	-0.1	0	0	-7	-1
Dollar index, (+) = $ appreciation		102.6	0.3	0	-1	0	1
Brent Crude Oil ($/barrel)		79.7	3.0	1	9	-5	4
VIX Index (%, change in pp)		12.7	0.3	-1	1	-6	0

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

Mature Markets

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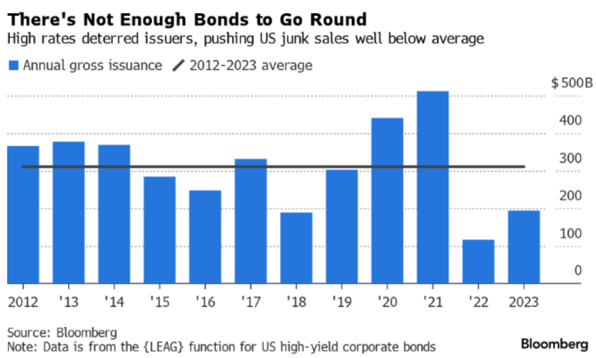
United States

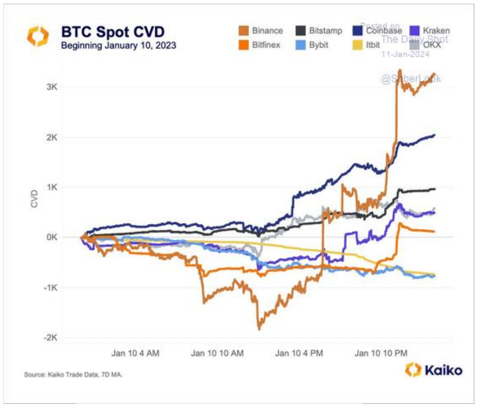
Treasury yields closed lower yesterday after investors digested a slightly higher-than-expected CPI data released in the morning. Investors appeared to believe that the latest CPI data will not change the "dovish pivot" narrative. Treasury 2-year yields declined by 12 bps with the yield curve steepening, and the market-implied Dec 2024 OIS rate was down by 14 bps to 3.785%, pricing more than six 25 bps rate cuts for this year. The S&P 500 index was almost unchanged. Meanwhile, Fed Cleveland President Mester said that it was premature to consider cutting interest rates as soon as March, and Richmond President Barkin reiterated that he is looking for more evidence that inflation is headed towards the target.

In contrast to the CPI release yesterday, **December PPI this morning was lower than expected**: -0.1% m/m (+1.0% y/y) versus +0.1% (+1.3%) expected. The index excluding food and energy was also lower: 0.0% m/m (+1.8% y/y) versus +0.2% m/m (+2.0% y/y) expected. In financial markets, **Treasury yields fell sharply immediately following the release, particularly at shorter maturities (2-years, -9 bps).**

US corporate bonds are expected to outperform on favorable supply-demand dynamics. As many corporate borrowers are opting to refinance or reduce debt rather than raise new cash for investment or acquisitions, the net supply of corporate bonds is not expected meet investor demand. According to Bloomberg, investment-grade corporate bond ETFs saw record inflows recently, offering higher yields than government bonds and lower default risk than high yield bonds. Meanwhile, credit fundamentals are deteriorating, as reflected by the steadily rising default rates. Rating agencies expect defaults to climb, even in a soft-landing scenario.



Bitcoin trading activities increased sharply on Wednesday following the SEC approval. JP Morgan analysts, however, are skeptical that a lot of fresh capital will enter the crypto space as a result of the spot bitcoin ETF approval. Instead, they expect a significant rotation from existing crypto vehicles to the newly created ETFs as fees and liquidity play a crucial role. Spot bitcoin ETFs are a cheaper alternative due to lower fees and safer as they are more regulated. Bitcoin fell after surging past $49,000 for the first time since December 2021 following the approval.

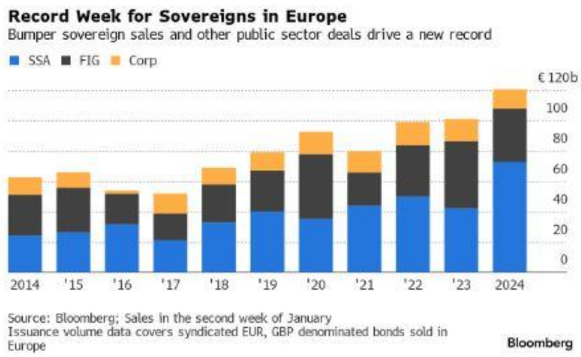


Source: The Daily Shot Brief

Euro Area

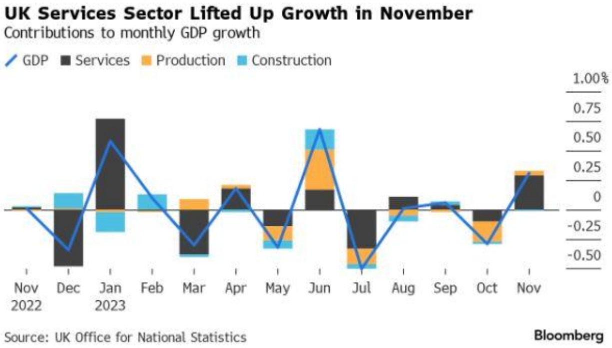
European equities rose modestly this morning. The euro was slightly weaker the dollar, trading at around 1.095. **Euro area sovereign yields were a touch lower with the 10-year bund yield (-2 bps) trading at 2.21%.** On the data front, final December CPI prints for France and Spain were in line with consensus expectations coming in at 4.1% y/y and 3.1% y/y, respectively. There was limited market reaction to the release. The next key data release for the euro area will be the German ZEW due on Tuesday.

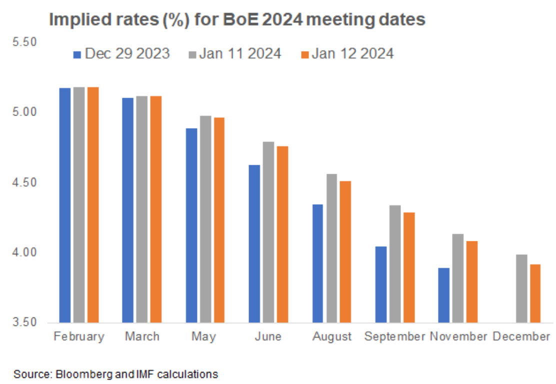
Separately, **Bloomberg reports that European government bond sales this week hit an all-time of high of €45 bn** with strong investor demand from foreign investors in the Middle East and Asia. Investors continue to rush to lock in higher yields before an expected easing in policy rates later this year. **Strategists at BofA believe that, even if the 2024 supply of euro area government bonds exceeds that of last year, it should be well absorbed given the level of demand from foreign investors, coupled with a more stable euro which removes some of the redenomination risk foreign investors may been concerned about** in the past.



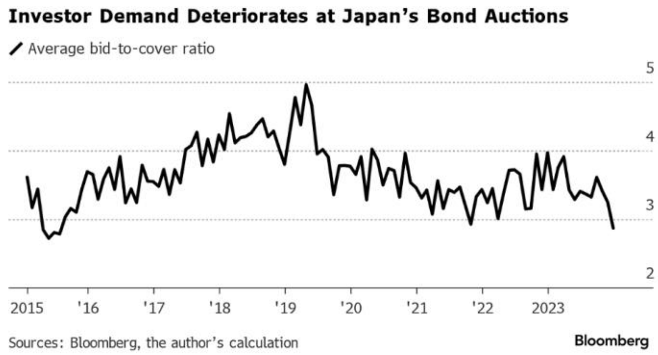
United Kingdom

The pound was weaker and gilt yields were modestly lower despite a stronger-than-expected monthly GDP print for November. Activity rose +0.3% m/m, versus +0.2% m/m expected and -0.3% m/m in the prior month, driven by growth in services and manufacturing of +0.4% which offset drags from the construction and energy sectors. Despite the positive outturn, **analysts at HSBC note that the risk of the UK entering a technical recession remains if activity for December prints negative**. Money markets continue to price in five quarter-point rate cuts, with the first cut expected in May, although this is somewhat less than the six rate cuts markets had been anticipating in December. Separately, industrial production data for November showed a 0.1% y/y decline vs an increase of 0.7% y/y expected and 0.4% y/y in the prior month.





Japan

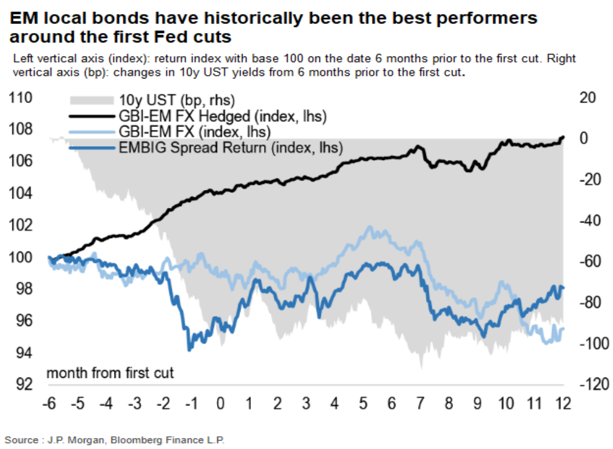


Bank of Japan (BOJ) officials are likely to discussed cutting their forecasts for growth and inflation at the next policy meeting. BOJ officials may consider a downward revision to the outlook for CPI excluding fresh food to 2.5% from 2.8% for the fiscal year (starting in April) due to a decline in oil prices. The growth outlook will also likely be marked down given weaker-than-expected 2023Q3 GDP data. **The 30-year JGB auction saw weaker demand than expected**, with analysts noting that major demand sources for long-end JGBs, particularly life insurers, were not interested in buying 30-year debt as yields are perceived as too low. Until the BOJ clarifies its monetary policy path, life insurers may remain cautions. Long-end JGB yields declined (10-year: -0.6 bp; 30-year: -0.3 bp), with the 10-year yield at 0.591%. The Japanese yen appreciated (+0.1%). **Japanese equities gained (NIKKEI: +1.5%), continuing their rally to make a new 34-year high.**

Emerging Markets back to top

Asian equities were mixed today. Hong Kong (-0.4%) and Chinese (CSI 300: -0.3%) equities declined, while share prices rose in India (+1.2%). **Asian currencies were also mixed,** trading in a tight range. **Local sovereign bond issuances drew robust demand this week,** including in Indonesia, Malaysia and Thailand as investors looked to lock in current yields. Most long-end government bond yields declined. **EMEA equity and currency markets were mixed while local currency bond yields were mostly lower.** The Hungarian equity market outperformed (+0.6%) while equities in Türkiye were almost unchanged on the day. Elsewhere on the central bank front**, Romania** is expected to keep its benchmark rate unchanged at 7.0%, in line with expectations. In **Latam**, currencies and equities broadly rallied after the US inflation print yesterday. Some currencies depreciated after the US data but rebounded back to gains as US rates ended the day pricing an even larger total amount of Fed cuts this year. Regional government yields also ended the day broadly lower, tracking US Treasury yields.

EM Local Bonds



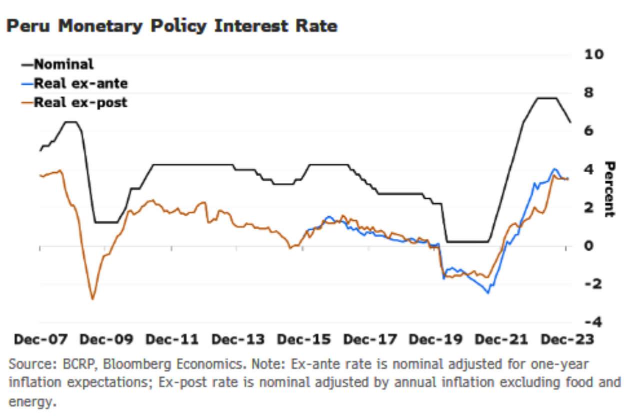
The Disinflation narrative is expected to drive returns for local currency bonds. According to a JP Morgan analysis, softer global growth and cooling inflation is expected to support returns for EM local currency bonds. The broad direction for EM bonds is also likely to be driven by expectations surrounding US rates, with the Fed's dovish pivot expected to drive market focus on global easing cycles through 1H 2024. An early Fed easing could also trigger a reassessment lower of EM rate forecasts, particularly if core US inflation continues to slide in Q1 of 2024. Historically, EM local bonds typically perform well during the first Fed cuts of an easing cycle, although it is less clear for the performance of EM FX and EM sovereign credit. Nonetheless, monetary policy cycles within EM are a key area of differentiation.

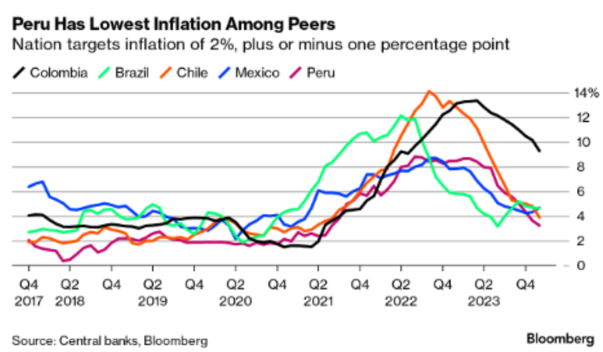
China

Markets expect a cut in the Medium-term Lending Facility (MLF) rate next Monday amid persistent deflationary pressures. Based on the latest Bloomberg survey, the MLF will likely be lowered by 10 bps to 2.40%. Meanwhile, deflation narrowed in December. Headline CPI fell 0.3% y/y (consensus: -0.4%), compared with a 0.5% decline in November. A smaller decline in CPI was driven by a smaller drag from food prices and a pickup in prices of non-food items. Meanwhile, PPI fell 2.7% y/y (consensus: -2.6%), compared with a 3.0% decline in November. PPI deflation continued on lower energy prices and weaker demand for some industrial products. Separately, **trade data improved more than expected in December.** Exports increased 2.3% y/y in dollar terms (consensus: +1.5%), supported by robust auto and tech exports. Imports also increased 0.2% y/y in dollar terms (consensus: -0.5%). Some analysts noted that sluggish imports were due to subdued processing trade as multinational firms are relocating out of China. Chinese equities declined (CSI 300: -0.3%; Hong Kong SAR-listed: -0.2%). The RMB was little changed at 7.17 yuan per dollar as the People's Bank of China continued fixing the daily RMB fixing stronger than expected; today's deviation from consensus amounted to 534 pips. Long-end CGB yields rose modestly (10-year: +1.7 bps).

Peru

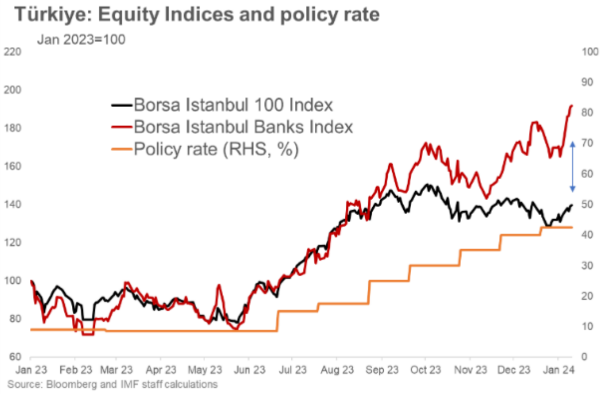
Peru's central bank cut policy rates to a 16-month low. The central bank lowered its policy rate to 6.5%, a fifth consecutive 25 bps cut that was in-line with analyst estimates. The MPC statement reiterated expectations for headline inflation to converge towards target over the next few months, although highlighting risks associated with climate factors (El Nino). The central bank maintained a cautious tone and emphasized that the cut does not imply that cuts should be expected at every meeting, with future decisions being data-dependent. Adjusted by inflation expectations (1-year ahead), the real ex-ante rate remains close to 3.6%, which remains above the neutral real rate that is estimated to be at 1.5%.





Türkiye

The central bank of Türkiye (CBT) is reportedly close to the end of its tightening cycle. According to Bloomberg, the central bank reportedly told investors that its interest rate tightening cycle would come to an end as soon as possible, given that interest rates are approaching levels that would set inflation on an easing path. However, Morgan Stanley analysts still expect another 250 bps hike at the upcoming policy meeting in January, to a 45% terminal rate. In the meantime, **the Turkish banking stock index continues to outperform the broader Turkish equity index.** Earlier this week BofA analysts argued that the banking sector is the best way for investors to position for the "normalization" of inflation, interest rates and the currency. Analysts noted in a report that investor interest in the Turkish banking sector is back to levels seen pre-2013. Current account data for November showed a current account deficit of $2.7 bn vs expectations of a $1.7 bn deficit.



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Global Financial Indicators

1/12/24 8:15 AM	Level: Last 12m	Level: Latest	Change: 1 Day	Change: 7 Days	Change: 30 Days	Change: 12 M	YTD
Equities					%		%
United States		4771	-0.1	2	3	20	0
Europe		4463	0.5	0	-2	8	-1
Japan		35577	1.5	7	8	36	6
China		3284	-0.3	-1	-2	-19	-4
Asia Ex Japan		64	0.7	-1	-1	-8	-3
Emerging Markets		39	0.4	-1	0	-5	-3
Interest Rates					basis points		
US 10y Yield		4.00	3.5	-4	-20	56	12
Germany 10y Yield		2.22	-1.9	6	-1	6	19
Japan 10y Yield		0.61	0.4	0	-11	10	-1
UK 10y Yield		3.83	-1.7	4	-14	49	29
Credit Spreads					basis points		
US Investment Grade		130	-1.5	-7	-7	-21	-3
US High Yield		394	-1.1	-9	-16	-51	9
Exchange Rates					%		
USD/Majors		102.55	0.3	0	-1	0	1
EUR/USD		1.09	-0.2	0	1	1	-1
USD/JPY		145.4	0.1	1	0	13	3
EM/USD		47.8	-0.1	0	0	-7	-1
Commodities					%		
Brent Crude Oil ($/barrel)		79.7	3.0	1	8	0	4
Industrials Metals (index)		136	-0.2	-1	2	-20	-4
Agriculture (index)		62	0.7	1	-4	-9	-2
Implied Volatility					%		
VIX Index (%, change in pp)		12.7	0.3	-0.6	0.7	-6.1	0.3
Global FX Volatility		7.7	0.0	-0.3	-0.3	-3.3	-0.4
EA Sovereign Spreads					10-Year spread vs. Germany (bps)		
Greece		106	-1.2	-10	-15	-84	3
Italy		157	0.3	-12	-20	-27	-10
Portugal		59	0.2	-6	-8	-32	-4
Spain		92	0.3	-7	-9	-7	-5

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

Emerging Market Financial Indicators

Last updated: 1/12/2024 8:13 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		7.17	0.0	-0.3	0	-6	-1		2.5	-1.8	-2	-14	-65	-5
Indonesia		15550	0.0	-0.2	0	-1	-1		6.7	-3.9	-4	-3	-9	18
India		83	0.1	0.3	1	-2	0		7.2	-4.1	-14	-16	(20.0)	-2
Philippines		56	0.1	-0.6	-1	-1	-1		5.7	21.0	-3	-25	-39	2
Thailand		35	0.0	-1.2	2	-6	-2		2.7	2.5	-8	-8	16	2
Malaysia		4.65	-0.1	0.2	1	-6	-1		3.8	0.6	-6	4	-16	8
Argentina		816	-0.1	-0.5	-55	-78	-1		81.1	44.0	-217	-622	-264	-525
Brazil		4.87	0.0	0.1	2	5	0		10.6	-3.2	-3	-32	-161	22
Chile		913	-0.1	-2.5	-4	-10	-3		4.9	-1.2	-14	-15	-9	1
Colombia		3913	0.4	-0.9	2	20	-1		7.6	0.0	-27	-55	-177	-7
Mexico		16.90	0.1	-0.1	2	11	0		8.5	1.0	-16	-34	44	5
Peru		3.7	-0.1	0.7	2	2	0		6.7	0.0	-15	-36	-104	3
Uruguay		39	0.3	0.2	0	1	-1		9.3	-17.8	-27	-41	-142	-27
Hungary		347	-0.4	-0.4	2	6	0		5.6	-8.0	-32	-63	-219	-22
Poland		3.99	-0.5	-0.3	1	8	-1		4.4	-0.2	-12	-13	-72	-6
Romania		4.5	-0.3	0.0	1	0	-1		6.2	-2.0	-15	-43	-110	-4
Russia		88.4	0.3	2.9	2	-23	1							
South Africa		18.7	-0.2	0.1	2	-10	-2		9.1	6.0	5	-13	53	0
Turkey		30.10	-0.3	-1.0	-4	-38	-2		26.8	-8.0	-138	3	1697	5
US (DXY; 5y UST)		103	0.3	0.1	-1	0	1		3.91	3.5	-9	-31	38	7

	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		3284	-0.3	-1	-2	-19	-4		163	5	9	-22	5
Indonesia		7241	0.3	-1	1	9	0		112	3	7	-60	16
India		72568	1.2	1	2	20	0		126	1	16	-29	10
Philippines		6643	0.4	0	3	-4	3		94	5	10	-51	14
Thailand		1414	0.4	-1	2	-16	0		0	0	0	0	0
Malaysia		1487	0.3	0	2	-1	2		92	4	7	-15	7
Argentina		1043924	-2.5	4	3	346	12		1929	-94	-18	-88	16
Brazil		130649	-0.2	-1	3	17	-3		212	-14	-3	-67	-3
Chile		6028	-0.5	0	2	16	-3		131	-7	6	-23	6
Colombia		1283	-0.4	1	12	-4	7		300	4	3	-83	29
Mexico		55439	0.2	0	2	3	-3		334	-17	-27	-43	0
Peru		25826	-0.1	1	17	12	-1		155	-5	6	-43	11
Hungary		63430	0.6	3	7	37	5		169	4	9	-81	20
Poland		76195	0.2	-1	-1	23	-3		108	-1	9	2	11
Romania		15813	0.5	3	4	28	3		216	-6	16	-60	15
South Africa		73707	-0.2	-1	1	-6	-4		336	2	-7	-17	28
Turkey		8001	1.3	5	3	61	7		347	6	1	-146	33
Ukraine		507	0.0	0	0	-1	0		3968	-161	318	-208	-36
EM total		39	0.3	-1	0	-5	-3		363	-3	4	-25	17

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

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