GLOBAL MARKETS ANALYSIS
Monetary and Capital Markets

Global Markets Monitor

MONDAY, JANUARY 8, 2024

LEAD EDITOR: SANJAY HAZARIKA

- **Markets price six Fed rate cuts over the next 12 months** (link)
- **Investor shorts in US dollar reach historic levels** (link)
- **Emerging markets issue more than $26bn of bonds in first week of year** (link)
- **Markets scale back expectations for Bank of England rate cuts** (link)
- **Turkish bank stocks rally on analyst upgrade** (link)

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Markets start year cautiously

Markets are down for the fourth day in five in January as caution replaces the euphoria seen in November and December. Global interest rates are higher as investors reassess the prospects of central bank rate cuts. Markets surged at the end of last year after the Fed indicated that it was done with rate hikes and would pivot to lower rates. However, worries about inflation, global conflicts and elections in many systemically important countries have scaled back the optimism seen at the end of 2023. Meanwhile, earnings season is scheduled to begin this week, with the big US banks among the first to report. There is a high degree of uncertainty about corporate profits, both for Q4 last year and the year ahead. In the euro area, German factory orders were weaker than expected, highlighting fears that Europe's biggest economy faces increasing challenges. In Asia, a sharp decline in Chinese technology shares dragged regional indexes lower. On a more positive note, oil prices fell on expectations that higher production in the US will offset OPEC+ supply cuts.

Key Global Financial Indicators

Last updated: 1/8/24 7:58 AM	Level		Change from Market Close				
	Last 12m	Latest	1 Day	7 Days	30 Days	12 M	YTD
Equities				%			%
S&P 500		4697	0.2	-2	2	21	-2
Eurostoxx 50		4463	0.0	-1	-1	11	-1
Nikkei 225		33377	0.3	0	3	29	0
MSCI EM		39	0.1	-2	1	-2	-2
Yields and Spreads				bps			
US 10y Yield		4.05	0.4	17	-18	49	17
Germany 10y Yield		2.20	4.1	17	-8	-1	17
EMBIG Sovereign Spread		402	-1	19	-2	-63	19
FX / Commodities / Volatility				%			
EM FX vs. USD, (+) = appreciation		47.8	-0.2	-1	0	-5	-1
Dollar index, (+) = $ appreciation		102.5	0.0	1	-1	-1	1
Brent Crude Oil ($/barrel)		76.8	-2.5	0	1	-2	0
VIX Index (%, change in pp)		13.9	0.5	1	2	-7	1

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

2023 in Review: Key Market Variables, 5pm December 29, 2023
Source: Bloomberg

Market Variable	Performance in 2023 (Local Currency)
S&P 500	+24.2%
Nasdaq	+43.4%
Euro Stoxx 600	+12.74%
Nikkei	+28.2%
Shanghai CSI 300	-11.4%
India Nifty 50	+20%
Brazil Bovespa	+22.3%
10-Year Treasury	Unchanged
10-Year Bund	-55 bps
10-Year JGB	+21 bps
Brent Crude Oil	-10%
Euro	+3.1%
Yen	-7%
Yuan	-2.9%

Most international equity markets had a good year in 2023, driven by expectations of central bank rate cuts, falling oil prices and government bond yields and a stronger than expected global economy. Optimism about artificial intelligence also played a role, especially in the US. China was the outlier, with the CSI index falling for a third consecutive year on economic worries. A weaker dollar was another tailwind for global markets, although the Yen and the Yuan lost ground versus the dollar. Most equity forecasts for 2024 are cautiously optimistic, although gains are expected to be much more modest than last year. The euro area and the UK are expected to fall into recession, but analysts are more optimistic about the US. Analysts think the biggest risks facing global markets are a resurgence in inflation, an unexpected slowdown in the US and the escalation of regional armed conflicts. Political risks could emerge around election results in the US and elsewhere, which could also have a negative impact on markets.

US inflation data will probably dominate the action this week, with CPI due on Thursday and PPI on Friday. Earnings season is due to start, with the big US banks led by JP Morgan the first to report their results for Q4 2023. Analysts forecast a good year for US financials, with the Fed expected to deliver multiple rate cuts and expectations of a steepening of the yield curve, which should help bank profits. The euro area is due to report on eurozone unemployment and industrial production in Germany. China will report its inflation data at the end of the week, while India is scheduled to report on industrial production. The UK reports on GDP on Friday. Poland is expected to stay on hold at 5.75% this week, while Peru is expected to cut by 25 bs to 6.5%. Korea is expected to stay on hold at 3.5%.

Mature Markets

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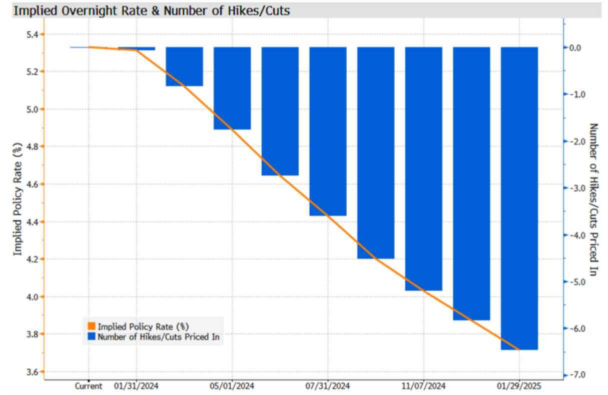
United States

The Fed Funds futures market is predicting six full rate cuts over the next 12 months. The pricing of options on Fed Funds futures implies that the policy rate could fall below 3.8% by next January. Friday's much weaker than expected ISM PMI data solidified rate cut expectations, with the previously robust services sector posting the largest decline. The PMI report overshadowed the strong jobs data reported earlier in the session. Treasury yields declined and equities rallied in the immediate aftermath of the later economic reports. However, both stocks and Treasuries gave up most of their gains by the end of the day, with Treasury yields higher and equities posting just fractional gains.

Fed Funds Futures Market: Forecast for Fed Rate Cuts

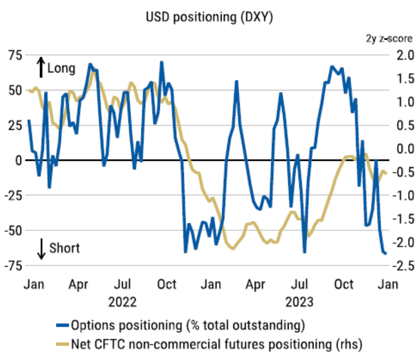


Source: Bloomberg

Foreign Exchange Markets

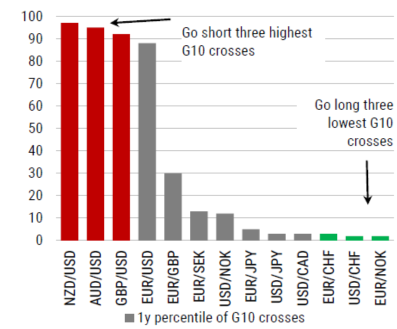
Investor short positions in the US dollar have reached historically high levels, according to research by Morgan Stanley. Short positions in the dollar have reached two-year z-scores of more than two standard deviations, an extreme move by historical standards. The dollar weakened for much of 2023, providing a tailwind to emerging markets and boosting risk sentiment overall. Investors are most long in the Swiss franc, euro, and Norwegian Krone. However, as risk-off sentiment took hold at the start of the new year, the dollar has appreciated significantly against most major currencies.

Exhibit 7:



Source: DTCC, Bloomberg, Macrobond, Morgan Stanley Research; Options data as of Monday, January 1; Futures data as of Tuesday, December 26. Note: Using options that were traded in the past three months and expire in the coming one month. Notionals are delta-adjusted. For methodology, see Assessing FX Positioning with Currency Options.

Exhibit 8:



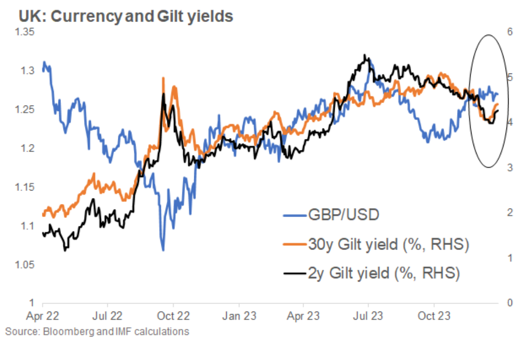
Source: Morgan Stanley Research; Data as of Monday, January 1. For methodology, see Assessing FX Positioning with Currency Options.

Euro Area

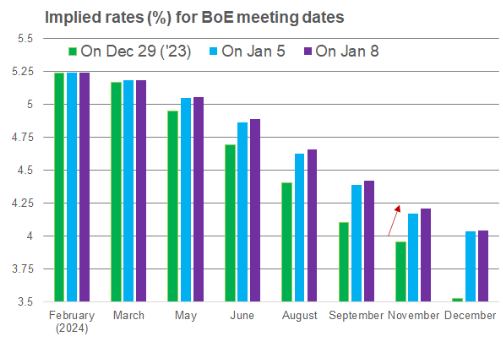
Euro area sovereign yields continue to edge higher while the euro was little changed against the dollar. This morning 10y bund yields were 3bps higher, trading at around 2.18% after ending last week roughly 13bps higher. Data released last week showed December euro-area flash inflation data in line with expectations, with the headline rate ticking up to 2.9% y/y (from 2.4% y/y), while core CPI continued to edge lower to 3.4% y/y (from 3.6% y/y). Markets adjusted expectations for ECB rate cuts and are now pricing in around a 45% chance of a 25bps rate cut in March, with roughly 145bps of cuts by the end of 2024, relative to the start of this year where market pricing suggested a roughly 53% chance of a rate cut in March and around 164bps of easting by year-end**.** The euro is trading at around 1.09 against the dollar**,** and CFTC data shown that EUR net long positions have increased for the second consecutive week. Stocks were lower. In other news, analysts think the Red Sea shipping disruptions will push up inflation, but to a limited extent.

United Kingdom

Gilt yields continued to rise as markets scaled back BOE rate cut expectations. Last week, Gilts led the bond sell-off in Europe, with the 10y gilt yield ending the week 25bps higher at around 3.79%. Contacts noted that yield moves were likely driven by strong data releases. Moreover, they also see much of the rally in Gilts toward the end of 2023 as overdone and expect higher rates going forward. Market are pricing in just 120bps of BoE rate cuts by the end of 2024, compared to the 170bps of rate cuts priced at the end of December 2023.



Source: Bloomberg and IMF calculations



Source: Bloomberg and IMF calculations

Emerging Markets

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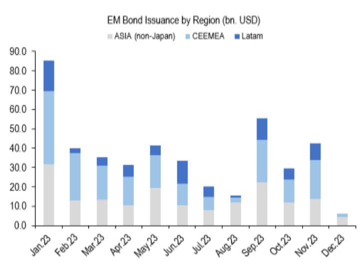
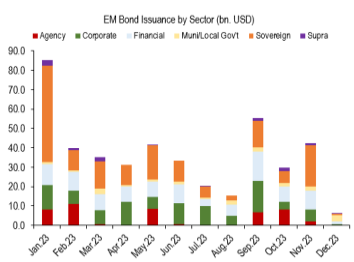
EMEA equity markets were mixed this morning, while currencies were slightly weaker against the euro and local currency sovereign debt yields were a touch higher. Economic data in the Czech Republic and Poland were weaker than expected, but the market impact was limited. **Most Asian equities declined, down 1.1% on net, led by Hong Kong (-1.9%) and China (CSI 300: -1.3%).** The Thai baht depreciated after the PM called on the central bank to cut rates. **Latin American currencies, local bonds and equities mostly declined in the first week of the year, mirroring AE market developments and in-line with broader EM movements.** Brazil's fiscal deficit was wider than expected.

Emerging Market Bond Issuance

EM issuers sold a substantial $26.2bn of hard currency bonds during the first week of 2024 with USD-denominated issuances totaling $19.6 bn. In terms of sectoral composition, $17.6bn were sovereign bonds, $5.5bn were corporate/financial bonds, $2.5bn were agency bonds and $0.5bn were local government bonds. Notable sovereign issuers include Hungary, Indonesia, Mexico, and Poland, offering fixed rate issuances with maturities spanning from 5 to 30 years. Markets dynamics remain supportive with EM investment grade USD bond spread remaining tight amidst lower yields relative to the preceding quarter. For 2023, EM hard currency bond issuance totaled $436 bn, up 26% compared to the prior year. Sovereigns accounted for 37.4% of total issuances for the year, followed by financials (22.5%) and corporates (22.2%).

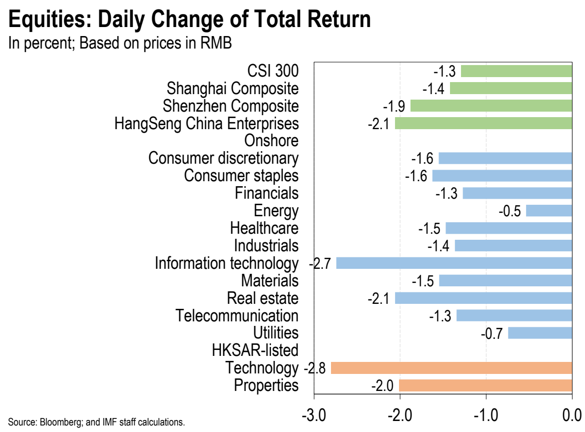




China

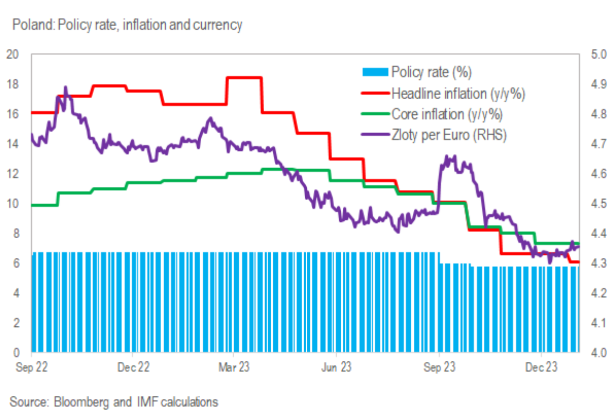
Chinese equities declined amid concerns over policy uncertainty and perceptions of inadequate macro policy support (CSI 300: -1.3%; Hong Kong SAR-listed: -2.3%). Investors remained worried about inadequate macro policy support as economic data continue to be weak. Long-end CGB yields continued falling as markets anticipated some policy rate cuts in coming months.

The Zhongzhi Enterprise Group filed for bankruptcy last week. The company said that it lacked the ability to repay its debt. An audit found that Zhongzhi' s debt amounted to around 420-460 billion RMB, compared with its assets of 200 billion RMB. The market impact has been muted so far, with spreads in the repo markets broadly stable. In addition, China Grand Automotive Services, one of the largest auto dealers, is also exploring debt repayment options. The company has a USD bond maturing at the end of the month. Analysts noted that the move highlighted efforts by Chinese high-yield USD bond issuers to preserve cash as they are struggling to refinance debt.



Poland

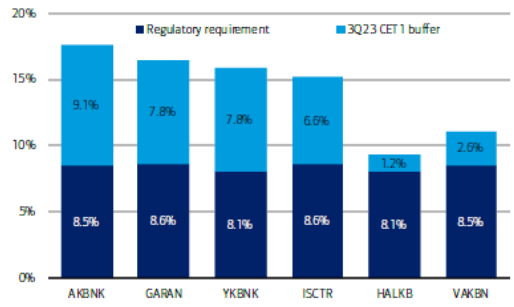
The National Bank of Poland is expected to keep rates unchanged at 5.75% at the policy meeting tomorrow as policy makers await further data about developments in domestic inflation. This would be the third consecutive month that rates remain on hold. Flash inflation data for December, released last week, showed headline inflation surprising on the downside (falling to 6.1% y/y versus 6.5% y/y expected and from 6.6% y/y in the prior month). **JPMorgan analysts expect the central bank to focus more on the sticky core inflation and therefore expects the central bank to keep rates unchanged until 4Q24, when analysts expect two 25bps rate cuts**.



Türkiye

Turkish banking stocks gained after analyst reports highlighted that investor interest in the Turkish banking sector is back to levels seen in 2013. In a note released earlier this morning, BofA analysts noted that investor interest in Turkish banks has increased as investors look to position for the "normalization" of inflation, interest rates and the currency. Analysts noted that long-only investors are following developments in Türkiye closely and believe that the country's banking sector provides the best way to gain exposure to this "normalization" theme. According to BofA, the Turkish banking sector has deleveraged and the private banks have sizeable CET1 capital buffers and have a demonstrated ability to manage a volatile interest rate environment. After the report was released, **Turkish bank stocks (Borsa Istanbul Banks index) was up around 6.3%. The wider Borsa Istanbul 100 Index was up 2.1%.**

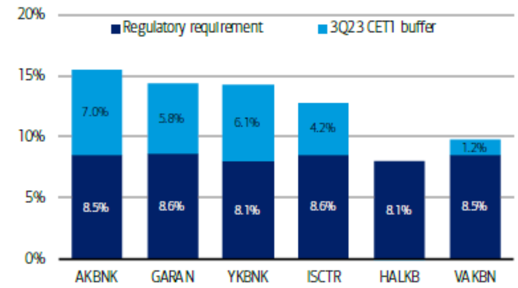
Exhibit 12: CET1 buffers with forbearance measures (consolidated)
Private banks' buffers above 6pp, highest at Akbank (9.1pp)



Source: Company financials, BofA Global Research

BofA GLOBAL RESEARCH

Exhibit 13: CET1 buffers without forbearance measures (consolidated)
Private banks' buffers above 4pp, highest at Akbank (7 pp)



Source: Company financials, BofA Global Research *Halkbank's adjusted capital ratios have not been communicated to the market.

BofA GLOBAL RESEARCH

This monitor is prepared under the guidance of Jason Wu (Assistant Director), Sheheryar Malik (Deputy Division Chief), Nassira Abbas (Deputy Division Chief), and Caio Ferreira (Deputy Division Chief). Fabio Cortes (Senior Economist), Sanjay Hazarika (Senior Financial Sector Expert), Esti Kemp (Financial Sector Expert-London Representative), Johannes S Kramer (New York Representative), Benjamin Mosk and Jeff Williams (Senior Financial Sector Expert) are the lead editors of this monitor. The contributors are Yingyuan Chen (Financial Sector Expert), Andrew Ferrante (Research Assistant), Deepali Gautam (Research Officer), Phakawa Jeasakul (IMF Resident Representative in Hong Kong SAR), Harrison Kraus (Research Assistant), Yiran Li (Research Assistant), Xiang-Li Lim (Financial Sector Expert),Kleopatra Nikolaou (Senior Financial Sector Expert), Natalia Novikova (IMF Resident Representative in Singapore), Mustafa Oguz Caylan (Research Officer), Silvia Ramirez (Senior Financial Sector Expert), Patrick Schneider (Financial Sector Expert), Ying Xu (Economist), Dmitry Yakovlev (Senior Research Officer), and Akihiko Yokoyama (Senior Financial Sector Expert). Javier Chang (Senior Administrative Coordinator), Lauren Kao (Administrative Coordinator), and Srujana Sammeta (Administrative Coordinator) are responsible for the word processing and production of this monitor.

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Global Financial Indicators

1/8/24 8:03 AM	Level: Last 12m	Level: Latest	Change: 1 Day	Change: 7 Days	Change: 30 Days	Change: 12 M	YTD
Equities			%				%
United States		4697	0.2	-2	2	21	-2
Europe		4463	0.0	-1	-1	11	-1
Japan		33377	0.3	0	3	29	0
China		3286	-1.3	-4	-3	-18	-4
Asia Ex Japan		65	0.0	-3	1	-5	-3
Emerging Markets		39	0.1	-2	1	-2	-2
Interest Rates			basis points				
US 10y Yield		4.05	0.4	17	-18	49	17
Germany 10y Yield		2.20	4.1	17	-8	-1	17
Japan 10y Yield		0.61	0.0	0	-16	11	0
UK 10y Yield		3.83	4.0	29	-21	36	29
Credit Spreads			basis points				
US Investment Grade		137	-0.9	3	-2	-25	3
US High Yield		402	-1.2	16	-9	-65	16
Exchange Rates			%				
USD/Majors		102.46	0.0	1	-1	-1	1
EUR/USD		1.09	0.0	-1	2	2	-1
USD/JPY		144.5	-0.1	3	0	10	2
EM/USD		47.8	-0.2	-1	0	-5	-1
Commodities			%				
Brent Crude Oil ($/barrel)		76.8	-2.5	0	1	1	0
Industrials Metals (index)		137	-0.9	-4	1	-16	-4
Agriculture (index)		61	-0.3	-2	-5	-9	-2
Implied Volatility			%				
VIX Index (%, change in pp)		13.9	0.5	1.4	1.5	-7.2	1.4
Global FX Volatility		8.1	0.0	-0.2	0.1	-2.7	-0.1
EA Sovereign Spreads			10-Year spread vs. Germany (bps)				
Greece		116	-0.7	12	-2	-100	12
Italy		169	0.0	2	-10	-32	2
Portugal		66	0.4	2	-2	-35	2
Spain		100	0.1	3	-3	-6	3

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

Emerging Market Financial Indicators

Last updated: 1/8/2024 8:06 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		7.16	-0.2	-0.9	0	-5	-1		2.5	2.8	0	-12	-54	0
Indonesia		15526	-0.1	-0.8	0	0	-1		6.7	4.5	23	12	-29	23
India		83	0.0	0.1	0	-1	0		7.3	-4.0	10	-3	(6.1)	8
Philippines		56	-0.2	-0.6	-1	-1	-1		5.7	-0.1	5	-18	-37	5
Thailand		35	-0.9	-1.8	1	-4	-2		2.8	-3.5	6	-6	22	6
Malaysia		4.65	0.1	-1.2	0	-6	-1		3.8	-3.8	10	9	-20	10
Argentina		813	-0.1	-0.6	-55	-78	-1		82.3	-100.4	-409	-1776	-422	-409
Brazil		4.90	-0.4	-0.9	1	7	-1		10.7	4.0	29	-22	-204	29
Chile		900	-1.1	-2.1	-3	-7	-2		5.0	-8.0	7	-6	-14	7
Colombia		3886	-0.2	-0.3	3	25	0		7.8	0.0	17	-6	-222	20
Mexico		16.90	-0.1	0.4	3	13	0		8.7	-2.0	21	-14	22	21
Peru		3.7	0.2	-0.3	1	3	0		6.9	0.7	18	-7	-104	18
Uruguay		39	0.2	-0.9	0	2	-1		9.5	-5.6	-6	-16	-121	-6
Hungary		345	0.2	0.7	3	7	1		5.9	0.0	11	-42	-207	11
Poland		3.97	0.2	-0.9	1	10	-1		4.6	3.8	9	6	-52	10
Romania		4.5	0.0	-0.8	2	1	-1		6.3	3.1	14	-17	-116	14
Russia		91.1	-0.1	-1.7	1	-24	-2							
South Africa		18.7	-0.2	-1.9	1	-10	-2		9.1	6.0	1	-12	49	1
Turkey		29.89	-0.3	-1.2	-3	-37	-1		27.2	-99.0	44	3	1862	44
US (DXY; 5y UST)		102	0.0	1.1	-2	-1	1		4.01	0.5	16	-23	31	16

	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		3286	-1.3	-4	-3	-18	-4		159	1	5	-20	1
Indonesia		7284	-0.9	0	2	9	0		117	21	0	-46	21
India		71355	-0.9	-1	2	17	-1		129	13	9	-15	13
Philippines		6609	-0.3	2	6	-3	2		95	15	-2	-36	15
Thailand		1418	-0.7	0	3	-16	0		0	0	0	0	0
Malaysia		1496	0.5	3	4	0	3		91	6	4	-13	6
Argentina		1055381	5.0	17	12	394	14		2003	90	65	-129	90
Brazil		132023	0.6	-2	4	21	-2		223	8	8	-59	8
Chile		6055	-0.5	-2	1	18	-2		134	9	7	-23	9
Colombia		1295	2.2	9	13	-2	8		294	23	-4	-85	23
Mexico		56193	1.4	-2	3	9	-2		344	10	-7	-52	10
Peru		25710	0.1	-1	17	15	-1		155	11	10	-50	11
Hungary		61409	-0.1	1	5	35	1		158	9	-10	-104	9
Poland		76597	0.0	-2	-1	28	-2		103	6	-6	20	6
Romania		15447	0.7	1	3	27	0		214	13	10	-88	13
South Africa		73981	-0.7	-4	0	-4	-4		327	19	-20	-48	19
Turkey		7783	2.0	4	-2	46	4		335	21	-23	-126	21
Ukraine		507	0.0	0	0	-1	0		4129	125	320	-36	125
EM total		39	-1.0	-2	1	-2	-2		362	17	-1	-28	17

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

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